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Joseph A. Pechman & Mark J. Mazur
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Beyond the Bell Breakup

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Fall Books — *Reviewed by Andy Stark, Ronald Berman, Jeremy Rabkin, Richard N. Langlois, James Piereson, Marc F. Plattner, R. Shep Melnick, Ronald Bailey, and William McGurn*

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Beyond the Bell breakup

PETER F. DRUCKER

SUCH discussion of the Bell System breakup as there has been—and there has been remarkably little—has centered mainly on the consequences for the shareholders and on share and bond prices. Yet few governmental actions since World War II will have such profound impact on American society, on American technology, and even on national security, as the antitrust suit against AT&T and the subsequent dissolution of the Bell System. Few so immediately affect every individual in the country. The antitrust suit and its sequel raise serious and disturbing questions about those twin pillars of the American political economy: regulation of business and antitrust.

Antitrust: the cynics' view

For antitrust cynics—and among economists they outnumber the "true believers" about ten to one—it is almost axiomatic that no major antitrust suit is ever brought until the alleged monopoly is already on the skids. For it is only then that competitors appear; their complaints that the monopoly is not collapsing fast enough push the antitrust machinery into action. And then the antitrust suit, the cynics contend, achieves the very opposite of what the anti-

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trust champions intend. By forcing the monopolist to stop defending yesterday, it restores his leadership position and gives him a near-monopoly on tomorrow.

This surely applies to America's most celebrated antitrust suit, the one that resulted in the breakup of John D. Rockefeller's Standard Oil Trust three quarters of a century ago. The "monopoly" which Standard Oil had was on kerosene, which had been *the* petroleum product until Henry Ford's Model T created a mass market for gasoline. In 1911, when Standard Oil was broken up, the gasoline market was still secondary but was growing fast, while kerosene was already in full decline and being replaced in all but rural areas by electric lights. And the gasoline market in the U.S.—and even more outside of it—was quickly taken over by aggressive newcomers such as Shell in England, Royal Dutch on the European continent, or Gulf and Texaco in the U.S. Yet Rockefeller stubbornly clung to kerosene, on which indeed Standard Oil had a near-monopoly worldwide. It was only after antitrust had succeeded in breaking up the Trust—in the process also dislodging the Rockefellers from active management—that the successor Standard Oil Companies were free to concentrate on gasoline. Ten years later, they had 70 to 80 percent of the U.S. gasoline market and almost 50 percent of the gasoline market in the outside world.

Similarly, IBM would never have achieved worldwide leadership in the computer market had an antitrust suit not been brought against the company in the mid-1940s for monopolizing the punch card. But by 1947, punch cards were already becoming obsolete. IBM had actually done most of the work needed to give it leadership in the technology of tomorrow: the computer. But its stubborn defense of the punch card paralyzed it to the point where it actually stifled research on computers and on marketing them. The antitrust suit enabled the proponents of tomorrow in IBM management, especially the founder's son, Thomas Watson, Jr., to shift the company's efforts from defending the past to attaining leadership in the future.

The next antitrust suit against IBM, the one the government finally abandoned in 1982 as hopelessly confused, was also brought at the very moment when minicomputers and personal computers first arose to challenge IBM's domination of the domestic market, and when the Japanese first became serious competitors in mainframe computers worldwide. This probably pushed IBM out of being content to be number one in mainframes, and into frantic efforts to do something it had earlier spurned: enter the market for small and personal computers.

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There is little doubt that the antitrust suit against AT&T (the Bell System) which ended last January with the split-up of the system, was similarly brought when the company's monopoly had already been breached. It certainly forced the company to give up defending yesterday. What we do not know yet is whether it will, as the earlier suits did, enable AT&T to dominate the communications market of tomorrow: The challenge is clearly there.

A phone in every room

Some 30 years ago, AT&T made the critical decision that would eventually lead to its being broken up. The company then ran its own Advanced Management School in Asbury Park, New Jersey, to which the "comers" in upper middle management were sent for several weeks of intensive training, usually just before being promoted into their first senior management jobs. The assignment for one of these classes during the final week at Asbury Park was to think through objectives and strategy for the Bell System, now that it had achieved its original and long-term objective of providing universal access to telephone service for everyone in the United States. (As it happened, I was the guest lecturer at Asbury Park that week and in charge of the sessions.) The assignment was to work out one recommendation for Bell System top management. But the class could not agree, and ended up—to everyone's intense annoyance—with a majority and a minority report.

The majority recommended that Bell change its basic posture in the market. While for more than 60 years the emphasis had been on providing everyone in the country with minimum service at lowest cost, the emphasis henceforth, the report proposed, should be on making people use their telephones as much as possible. This would mean pushing extensions in addition to the single telephone on the wall of the kitchen. It would mean selling more than one line to a customer (an extra phone for teenage children, for instance). It would also mean making the phone "interior decoration" rather than "utility"—"princess phones," for instance, or phones in colors other than black.

"All this is necessary," the minority agreed, "but it's not nearly enough. In fact, it's only rear-guard action and good for—at most—20 years. The traditional telephone market is saturated; let's face it. The growth, and it is already fast and speeding up, is in long distance and in transmitting signals other than voice such as television programs and computer data. What is needed in addition to hard selling of traditional local service is a basic change in policy.

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Indeed, what is needed is a redefinition of the 'system.' We have always defined it as local services connected to each other by long distance lines. We now need to redefine 'system' as a national and increasingly international information processor with local outlets. Specifically, this means first changing the basic pricing policy. Traditionally, we have priced so as to give the local subscriber the lowest possible cost while long distance users have paid a good deal more than the full cost of interconnection and of access to the local user. This way, long distance has been priced way above cost, and has in effect heavily subsidized local service. This needs to be changed so that the local subscriber pays the full cost and pays for access to the network. And then we ought to shift from having telephone rates regulated by 48 states, each only concerned with getting minimum service at minimum cost for local subscribers, to national regulation; for instance by the Federal Communications Commission, with the emphasis on getting optimum national service at the lowest cost to our nation. Our traditional policies were rational when local service was our first priority and the growth sector. It is becoming deleterious to the company as well as to the nation, now that the growth opportunities have changed."

Bell System's top management took these recommendations very seriously and studied them in depth. In the end, it decided to adopt the majority report. It was, we know by hindsight, the wrong decision. But there probably was no choice. To go along with the minority would have meant 48 battles with 48 state public utility commissions. Moreover, thousands of Bell Telephone people throughout the country had been inculcated for years with the local-service creed, and would have resisted any change. As it was, they strenuously resisted even the majority recommendation. "I have always been proud to provide public service and now they want me to be a huckster," one Bell System friend said when he saw the first phones in "decorator" colors. Another friend, the Chief Engineer for one of the operating companies, had been complaining for years that his four teen-aged children monopolized the phone in his home. But when he heard that his company was going to push separate "teenager lines," he exclaimed, "This is immoral," and immediately took early retirement.

There also did not seem to be any risk in at least postponing the shift in emphasis from local service to the fast-growing, non-local services. Bell, after all, was regulated. Thus it was considered in those days to be immune to antitrust, and to be able to exclude all would-be competitors. It was an inevitable decision, but the wrong one.

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The short-sighted hard sell

The hard-sell campaign which the majority had recommended became a tremendous success. Within ten years it converted the home telephone from a "utility" into a "convenience," if not into "fashion" and "glamor." Few marketing campaigns in American history have been nearly so successful. Ironically, this great success in the end seriously damaged AT&T. It created a debilitating conflict between customer expectations and regulatory reality. AT&T's marketing campaign made customers avid for novelty, for rapid change, for new features. But the regulatory realities—largely a reflection of AT&T's earlier values—resisted novelty, rapid change, and new features. All 48 state regulatory commissions in the continental U.S. had long ago been taught by AT&T that their job was to ensure universal access to minimum telephone service at lowest cost. This meant, specifically, that AT&T was not permitted to write off equipment still in good physical condition, even though technically obsolescent, unfashionable, or "basic" rather than "sophisticated." AT&T's campaign created a market for rapid change in telephone equipment, whether receivers or switchboards. But AT&T kept hundreds of thousands—perhaps even millions—of obsolete models that were older but still perfectly serviceable and therefore could not be written off or junked. And so AT&T found itself caught between not satisfying the very demand it had worked hard to create, and taking enormous losses on old equipment that might have endangered its financial integrity. Estimates of the write-off run into the billions. AT&T, understandably trying to hedge, only created a market for potential competitors.

At the same time, the forecast of the minority report proved correct: Non-local service, long distance telephoning, television transmission, and data transmission grew exponentially. In total numbers, calls within local areas still outnumber non-local calls. But both in demands on the system and in revenues, non-local services became, around 1970, the telephone system's center of gravity and its dominant, if not its only, growth sector. By now, Americans spend two dollars on long distance calls for every dollar they spend on local service. For the subsidized local subscriber, this was good news. But it also meant that non-local rates, and especially long distance rates, became increasingly divorced from costs, all the more so as the rapid rise in the volume of non-local traffic brought about a drastic reduction in its costs. AT&T did the intelligent thing: It offered large discounts to volume users. But this only increased AT&T's vulnerability, for it meant that anyone able to become a

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wholesaler—that is, anyone who could place enough individual long distance calls to qualify for the wholesale discount—could underbid AT&T's rates, and still make a handsome profit.

Finally, telecommunications technology exploded—largely as a result of the scientific contributions of AT&T's own Bell Labs. The transistor, switching theory, and information theory all came out of Bell Labs in the 1950s, and so did a good deal of computer logic and computer design. As a result of these breakthroughs, the telephone has virtually disappeared as unique technology. From AT&T's vantage point, the computer—for instance, in an office switchboard or in a central station—is an adjunct to the telephone; from the vantage point of an IBM, the telephone is simply a computer accessory.

No monopoly in history has ever survived even one such change, let alone several. If competition is forbidden by law, it comes in through a black market, but it comes in. Sooner or later, and usually sooner, the law is then changed one way or another. This is exactly what happened to AT&T. "Extensions" into which phones can be plugged had been quite rare; AT&T's big market push in the 1960s made them commonplace. This then created the market for competitors who, at first semi-legally, offered "decorator phones," "fun phones," and other, still officially forbidden, attachments. Then competition moved in on the office switchboard. AT&T had spent millions to develop electro-mechanical switchboards to take the place of the old, manually operated ones. But the competition offered computerized switchboards that leapfrogged over AT&T's equipment. The technology to do so had come from AT&T. But because of its inability to write off, let alone to junk, old equipment that had become technically obsolete while remaining in perfect physical condition, AT&T had to stick with electro-mechanical —that is, outdated—instruments. Finally wholesalers came in —MCI, Sprint, and a host of others—who offered long distance service to individual subscribers at 30 to 50 percent below AT&T's rates. AT&T invoked its traditional right as a regulated monopoly to keep these competitors out. But the courts, reversing a century of decisions and long-settled legal doctrine, ruled in case after case that a regulated industry is not exempt from antitrust, and that AT&T could not discriminate against competitors, ban their equipment, or penalize competitors' products in any way. In one important area, the impact on AT&T was immediate and substantial. In 1960, AT&T supplied almost all of the office switchboards used in America. Its share of the switchboard market now is less than one

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third, with the bulk of new equipment being supplied by companies like ROLM that began as computer manufacturers.

The biggest loss has been in long distance. As late as 1981, AT&T's Long Lines Department still handled 90 percent of all long distance calls in the country. By the middle of 1984, its share had dropped to 60 percent. Above all, AT&T has lost the most profitable market segments: The larger users increasingly either build their own system to link their plants and offices throughout the nation, or switch to telephone discounters such as MCI and Sprint.

From "Ma Bell" to "Monster Bell"

AT&T was thus increasingly forced on the defensive, and increasingly trapped between the need to maintain high long distance rates to subsidize local service, and the need to cut long distance rates to stanch the bleeding. Still, AT&T might have survived had it not been for inflation. The inflation of the 1970s eroded both the financial and the political base of the Bell System. And it undermined AT&T's self-confidence.

Employees within AT&T's own operations rarely know that their company has been one of the biggest non-governmental financial institutions in the world. Not only has the company been the capital markets' heaviest borrower year in and year out, for the telephone business is highly capital intensive. AT&T has also been the country's biggest lender. It has had to finance every single telephone subscriber for many years.

Traditionally, the subscriber did not buy the telephone connection to his home or his place of business, nor did he buy the equipment. The telephone company furnished both and was repaid out of operating revenues. And it took an average of five or six years until the subscriber's payments fully reimbursed the telephone company for the installation investment. Originally this was necessary; very few people in the telephone's early years would have been willing or able to pay the fairly large sums needed to get service. But in the years before World War I, Theodore Vail—AT&T's president from 1905 until his death in 1920 and the architect of the Bell System—turned this necessity into virtue and profit. He realized that AT&T could borrow at far lower interest rates than an individual possibly could; historically, AT&T has paid between 3 and 4 percent for its money. AT&T could thus finance the customer at a very low rate —4.5 to 5.5 percent on historical average—and yet make a handsome profit. This not only gave AT&T tremendous financial strength

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and security; it also enabled the company to lower rates for local service even more. Thus everybody profited.

But this very best of all possible financial worlds came to a rude end when the inflation of the 1970s pushed the interest rates AT&T had to pay to 13, 14, and 15 percent. While the interest rate to AT&T changed, the rate to the telephone subscriber remained frozen. Financing the subscriber then became a dangerous drain. Market growth—that is, new subscribers applying for service—became a threat, which explains why the Bell Companies have been doing worst where population has been growing fastest (as in southern California). Despite its automation, the telephone is still quite labor-intensive. And so, as inflation pushed up wages, AT&T and its operating companies were forced to ask for higher rates. But because financing of new subscribers—and additional installations for old subscribers as well—turned a riskless profit-making venture into a big financial loss, AT&T was forced to ask for even higher rate increases well beyond the rate of inflation.

In most parts of the country and for most services, the telephone, adjusted for inflation, still costs a good deal less than it did in 1950 or perhaps even in 1960. And American telephone service is still cheaper than telephone service anywhere else, with the possible exception of Canada. But for more than 60 years, the American public had known only declining telephone rates—and local subscriber rates had been declining both the fastest and the most consistently. Now, all of a sudden, telephone rates were going up, and local service rates were going up the fastest.

There surely has been far less "public uproar" over rising telephone rates than newspaper stories and TV commentators have reported. For the most part, the public contented itself with writing a few letters to the editor. But the political impact was considerable. Governors, state legislators, and public utility commissioners realized that they could get headlines and gain popularity by publicly resisting requests for higher telephone rates and denouncing the "telephone monopoly."

The psychological effect on the people at AT&T was devastating. Big companies—and big institutions generally, including universities, hospitals, and labor unions—tend to suffer from the dangerous delusion that the customer "loves" them. They are then shocked when they find out that a totally unsentimental and totally ungrateful customer only asks: "What will you do for me tomorrow?" But no institution in the U.S.—certainly no other business—has been so concerned with its standing in public opinion and so

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convinced of its being "loved" as the Bell Telephone System. This was by no means confined to top management. The lower ranks were even more deeply imbued with the Bell mystique.

And so the fairly mild protests against AT&T and its operating companies, protests which at General Motors would probably have been mistaken for expressions of endearment, came to the telephone employees as rejection by the beloved. A good many middle-management people I know in the Bell System feel as if their lives had been in vain. They had devoted their entire careers to serving the public, only to be attacked as greedy and reviled as profiteers. All along they had been confident of the public's support, and now, when for the first time they needed the public in a time of financial erosion and increasing competition, the public was turning against them.

It was just then, when all the traditional foundations of the Bell System were tottering, that the Justice department, on November 21, 1974, brought an antitrust suit asking for the breakup of the Bell Telephone System.

Breakup . . . without a fight

The AT&T suit has been documented more fully than any other antitrust suit in American history.[1] Yet it is full of puzzles.

It is reasonably certain that the suit was brought only because of the political vacuum in the White House at the end of the Nixon presidency, which freed the antitrust lawyers in the Justice department of political restraints. But why did the government pursue the suit? A Presidential Commission in the Carter administration condemned it as contrary to the national interest. Half a dozen members of the Ford, Carter, and Reagan cabinets recommended that it be dropped. And the Pentagon said publicly, on more than one occasion, that a standardized national telephone system under unified central management is absolutely essential for defense, and must not be broken up. Yet neither Ford, nor Carter, nor Reagan did anything to stop the suit. Why?

The Justice department, for its part, did little to push the suit. It waited six years, until January 1981, before bringing the suit to trial. And then it immediately adjourned the trial in the hope of a

[1] By Alvin von Auw, who for twelve years until his retirement at the end of 1981 was AT&T Vice President and Assistant to the Chairman. His book, *Heritage and Destiny: Reflections on the Bell System Transition* (New York: Praeger, 1983), reprints many of the government's and the company's briefs, internal memoranda, transcripts of meetings, and so on. It is probably the best record of what really goes on in a big organization and inside its top management, and is fascinating.

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settlement offer from the company. The only rational explanation is that the higher-ups in the antitrust division were under pressure from their own "true believers" to bring the suit, but expected to lose it.

AT&T's behavior was equally puzzling. AT&T has worked harder on public relations than any other large corporation in America. Yet its efforts to mobilize public opinion through the close contacts it had built up over the years with newspapers, local politicians, and academics were pathetically inadequate. Bell System's executives, as the von Auw book shows, knew from the very beginning that much higher rates for those least able to afford them, the individual subscribers, would inevitably result from separating local from long distance service, which was the antitrust division's first and central demand. Indeed, anyone on the outside, even if only superficially acquainted with the economics of the telephone, knew this. Yet I know of no attempt to alert customers or even the various public utility commissions—nor does von Auw's book mention any. Bell System management also knew—it was again obvious—that any change would mean both substantial layoffs and sharp wage reductions for Bell System workers. Like all protected industries, the Bell System was able to pass on wage increases to its customers, and thus had been forced to keep both employment and wages artificially high. Yet apparently no attempt was made to enlist the 600,000 Bell workers or their union, the Communications Workers of America, on the company's side in opposition to the antitrust suit. Nor did the union itself say one word about the suit that so clearly endangered it—perhaps even its very survival—even though opposition from the pro-union members of the Congress would almost certainly have put a fast stop to the suit. And Bell System management never, it seems, publicized the strong Pentagon protest. And yet, as the von Auw book documents conclusively, Bell System top management was emotionally committed to fighting the antitrust suit all the way without making any concessions, and considered the suit to be both totally without merit and totally immoral. Indeed, judging from the documents in the von Auw book, top management in AT&T was preoccupied for several years with fighting the suit and had time for little else. Had Bell's top management lost its nerve? Was it so overcome with its vicissitudes, and especially by its seeming rejection by the American public, as to have become virtually paralyzed?

All of a sudden, in the closing weeks of 1981, Bell capitulated. It voluntarily offered to divest itself of the operating companies and to restrict itself to long distance and overseas operations, to the manu-

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facture and sale of telephone equipment, and to telecommunications research. The decision came without any warning and as a surprise to everyone in the Bell System, where it was then generally believed that the suit would surely drag on until around 1990, and would finally be fought out in the Supreme Court. Instead, Bell accepted voluntarily most of what antitrust had asked for.

The only rational explanation for the sudden about-face of the Bell System top management is that it found itself forced to redefine its own role and function. Since Theodore Vail's days in the early years of the century, AT&T has always seen itself as a "private company in the public service" rather than as a "private business." It was in this tradition, as the documents in the von Auw book clearly show, that Bell System top management felt itself duty-bound to fight the government antitrust suit as likely to damage the American economy, to penalize the poor, and to endanger America's technological leadership (as we shall see, all perfectly legitimate concerns). But then, for six long years, no one in the public noticed their plight and came to their support—neither the media nor the administration nor the public utility commissions of the states, nor the labor union, nor even the Pentagon, which probably had more at stake in the antitrust suit than anybody else. And then, though one can only guess, the Bell System top management people might have said to themselves, "If no one accepts us as defenders of the public interest, we have to do what the law tells us is our duty, that is, look after the interests of the company and its shareholders."

And so, once they had capitulated, they acted with amazing speed. Two years later, on January 1, 1984, the Bell System breakup was complete. AT&T accepted competition in long distance service, and in providing instruments and equipment to the public. In return, AT&T was relieved of all responsibility for local service and with it of the responsibility to subsidize the local subscriber. This responsibility is now being shifted to seven independent large regional companies. Neither the operating companies nor AT&T have to finance the customer's equipment any longer. They are now free to sell it. AT&T will eventually be free to set long distance rates and thereby to fight back against competition that its former rate structure created and indeed subsidized. For the first time since the 1920s, when earlier antitrust fears made the Bell System sell its European manufacturing operations (after which it confined itself to North America, and since the 1950s to the Continental U.S.), AT&T can compete worldwide. And it can engage in any business whatever, for instance selling computers and office equipment.

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But what specifically is the future for the operating companies and for AT&T? And what does the Bell breakup mean for the American telephone user and for American national security?

Regional difficulties

Every one of the new regional companies into which the Bell System has been split has committed itself publicly to bold entrepreneurship and aggressive marketing—for instance, to leadership in cable television. But the future of the operating companies will depend on something far more mundane: on their ability to succeed in the traditional business of offering common carrier service for a diversity of electronic messages going from one telephone instrument to another.

The former Bell System operating companies will all face several highly turbulent years fighting for the rate increases they need to survive. In many areas and for many classes of service, rates will double. And this will be all the more difficult politically because the antitrust suit promised, of course, that the consumer would greatly benefit from the breakup of the Bell monopoly. But in addition to losing the subsidy from long distance, the operating companies will have to pay a good deal more for the money they need now that they are no longer sheltered monopolies. And they will have to raise very large sums of money for equipment and facilities.

Second, they will have to complete the shift they have only begun: from owning, leasing, and installing equipment to selling it. Within ten years, the operating companies will have to transfer to the customer the burden of paying for telephone instruments, and also for the connection from the nearest telephone line to the user's building. They will not be able to finance equipment for the user, nor be able to afford the labor costs of installing and repairing equipment. Eventually this may lead to a new and profitable business—if and when interest rates come down. The Bell Companies may be able to start finance companies which will offer the consumer five to eight year installment finance on attractive terms. But this is well into the future. In the meantime, companies will have to persuade both the public and the public utility commissions of the 48 continental states (for AT&T does not operate in Alaska and Hawaii) to allow them to withdraw from a service consumers and public utility commissions have been taking for granted for a century. We will thus inevitably see more attempts to guarantee low cost telephone service for the poor, such as the recent California Universal Telephone Law. But this simply means that the subsidy to the local users that business

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—that is, high volume long distance users—formerly paid will now be provided by the taxpayer.

But perhaps even more difficult will be the labor problem. What the operating companies need is something like a one-quarter to one-third reduction in total employment and a one-quarter to one-third reduction in hourly labor rates and in the total labor cost burden. Historically, public utility commissions have automatically allowed the telephone company to pass along all employment costs and all wage increases. This is unlikely to continue, in part because rates have become highly politicized, in part however because unions —especially large, mass production unions—have lost so much of their political power. Elected officials, such as Public Utility Commissioners, are now clearly more afraid of taxpayers than they are of the union vote. And Bell workers, as employees of a protected industry, have achieved wage benefit levels higher than Bell's competitors pay.

There are 600,000 members of the Communications Workers of America, and any reduction of staff and pay will hit hardest at installers and repairmen, the most highly paid but also the most completely unionized of all Bell workers. Yet they know that striking is not going to help them much; telephone service is so highly automated that most subscribers would not notice even a very long strike. Labor relations, in other words, are bound to be bitter on both sides, and turbulent.

Each of these tasks is difficult and represents a complete break with Bell System tradition. Each is going to cause raucous quarrels, bitterness, and bad publicity. But each will have to be tackled.

Learning to compete

It is far more difficult to predict the future of AT&T, the former parent of the Bell System, now that it has been released from all parental responsibility—providing local service, installing and financing equipment—and from restrictions on the sale and pricing of its products, and the restriction to do business only within the continental U.S. Or, rather, one has to predict "futures." For AT&T is not one, but four major businesses, each quite different though interlocked with the others.

First there is non-local telephone service. For some additional time, AT&T may still labor under a fairly heavy competitive penalty. The competing long distance services have lobbied, and with considerable success, to delay for a year or two AT&T's proposal to levy "access charges" on local telephones, charges that would have

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curtailed the competitors' rate advantage and have enabled AT&T to cut its own long distance rates fast and sharply. But even after the penalty is eventually removed, AT&T will face an uphill struggle to get back the long distance users it has lost, and especially the big ones among them. Whether it can ever regain its leadership is questionable. A good many of the best long distance customers, the very large ones such as the big multi-plant companies or the very big banks, have been pushed by AT&T's high long distance rates into building their own private telephone systems. And so have several of the competing services. The biggest, MCI, is actually planning to build its own trans-Atlantic circuits.

Even murkier is the future of AT&T's second unit, the huge manufacturing subsidiary, Western Electric. In number of employees (150,000), Western Electric ranks tenth among American manufacturing companies; in sales ($12 billion) it ranks twenty-second. But in profitability it ranks well below 300, with a laughable return of 2.5 percent on sales and a return of 7 percent on assets—less than one third of such comparable engineering companies as General Electric or IBM, and a good deal less than half of the minimum return an engineering company needs to defray its cost of capital. But, of course, Western Electric never had to compete, as the Bell System bought everything it turned out. It never was run for profit, but as a supplier to the operating companies. And it never had any credit losses, or inventories to write off, or marketing expenses.

Now, almost overnight, Western Electric will have to compete for every order it gets. Under the antitrust settlement, the operating companies have to consider every supplier rather than favor one of them—and the state Public Utility Commissions will make very sure they do. All of the world's traditional telephone equipment makers —Siemens from Germany, Ericsson from Sweden, the ITT companies from this country, Great Britain, Germany, France and Belgium, NEC from Japan, and half a dozen others—are already in the American market hawking their wares to Ma Bell's orphans. And the mightiest and the most aggressive new competitor, IBM, is moving full speed into the telephone business. It has bought a substantial interest in ROLM, Western Electric's most dangerous competitor in the switchboard field, and another big holding in Intel, a leading manufacturer of the semi-conductors that go into telephones and telephone switch gear.

On top of all this, Western Electric must break into a world market that it once dominated, but from which it retreated 60 years ago. It needs the volume. As long as Western Electric had to make

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everything the Bell Companies bought, and as long as the companies in turn had to buy everything Western Electric made, Western Electric had to produce an unknown but very large number of items that were neither the right products for its plants nor even remotely profitable. Obviously, it will not be able to sell these products from now on. And where, except in the export market, could it possibly get the volume to fill this capacity? The developing world is *the* market for truly advanced telecommunications equipment today, simply because developing countries (such as Singapore, Colombia, Kuwait) do not have large quantities of older equipment still functioning that would be too good to replace overnight. Thus, Western Electric has energetically moved out of the U.S. into a partnership with, for example, Olivetti, the large Italian office equipment and minicomputer maker. Yet the world market is already oversupplied with telephone manufacturers, and the big telephone orders —typically orders from national governments, of course—require the kind of financial encouragement that large exporters in Europe or Japan get from their governments as a matter of national policy, but which does not exist in the U.S.

Western Electric has formidable assets in design, in engineering, in manufacturing—in everything, in fact, but marketing. It also has no choice but to try. But still there is no evidence that a frog can turn into a prince, and that is roughly what Western Electric is trying to do.

Does Bell Labs have a future?

The third of AT&T's main units and the best known, Bell Telephone Laboratories, poses the most difficult decision. When the Bell System split itself up, top management announced that there would be no change whatever in the role and function of the System's famed Bell Labs. But this, no matter how sincerely intended, is unlikely. Indeed, Bell Labs faces the most radical change in its history and its mission.

However, the antitrust settlement is only a minor factor in this, only the trigger. Bell Labs in its traditional form had actually been increasingly untenable for a long period of time, largely as a result of its own successes and contributions. Bell Laboratories' discoveries and inventions have largely created modern "electronics"; they thereby eliminated the "telephone" as a distinct technology. To do what Bell Labs was founded to do in 1925, and did magnificently for 40 years—that is, to produce *all* the science and technology that a telephone needs—had become literally impossible. No one lab, no

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matter how good or how big, can possibly do this any more. Everything in electronics, but also in solid state or molecular physics, in metallurgy or in plastics, in crystallography or in computer sciences, and in a host of other disciplines, has a direct and immediate application to telephoning. And conversely, even the world's biggest telephone system is not large enough as an outlet for the discoveries and inventions that come out of Bell Labs. Indeed, in a wide array of areas, from the transistor to fiber optics, and from switching theory to computer logic, the Bell System has been no more adequate as a conduit for Bell Labs' scientific contributions than an eye dropper would be to channel a mountain freshet. The main users have been others—that is, non-telephone industries—with Bell Labs getting little out of its contributions other than an occasional footnote in a scientific paper.

The antitrust suit probably delayed by a decade the tackling of this problem. But now it must be faced. Under the new arrangement Bell Laboratories' expenses can no longer be paid for by the operating companies. They can, of course, contract with Bell Labs for specific work if they so choose, but they no longer have an obligation to contribute. Considering the pressures on the operating companies to hold down costs, the 48 public utility commissions are certain to look with a very skeptical eye on any payment from the operating company in their state to Bell Labs. Bell Labs, in other words, suddenly may have only a fraction of its former economic base.

For several years it had been clear that Bell Labs could go in two directions. It could become a standard industrial lab of a big engineering company, comparable to the labs of GE, RCA or DuPont. This does not necessarily condemn it to mediocrity; the GE lab can match its Nobel Prize winners with any scientific institution in the world. But it is a very different role from that to which Bell Labs has been accustomed.

And then there would be a far bolder, but also far riskier course: to convert Bell Labs into something totally new, a worldwide *scientific* laboratory in telecommunications and electronics, in business for itself, a lab that would aim at making a profit by taking research assignments from whoever is willing to pay for them, by developing its own patents and products to sell and to license, and so on. AT&T would still be the parent company of such a Bell Lab, but otherwise it would be just another client and would be dealt with at arm's length. Nothing like this has ever been done. And no one knows whether it could succeed. But it clearly is the alternative to Bell

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Labs' becoming another, though very good, industrial laboratory subordinated to a major manufacturing company.

The Bell System breakup, which deprived it of its financial base in the operating companies, surely tips the balance toward Bell Labs' becoming Western Electric's research and development department. It is hardly coincidence that one of the first organizational changes AT&T made after the breakup of the Bell System on January 1, 1984, was to put Bell Labs into the same organizational group as Western Electric and to subordinate it to the same management.

The risk to defense communications

Almost no one, so far, has publicly even mentioned AT&T's fourth major business: national defense communication. Yet it may be the most important, and the one most severely affected by the breakup of the Bell System.

Communications, everyone agrees, are the nerve system of modern defense. If communications do not function, defense collapses. Communications, everyone further agrees, are the one major area where the U.S. has so far enjoyed unquestionable superiority. Everyone also agrees that an enormous amount of work and effort will be needed simply to maintain our defense communications. For we now know that what we have is highly vulnerable to magnetic fields created by explosions in space. For "defense communications in the U.S.," read AT&T. What gave the U.S. its superiority in defense communications were precisely the features of the Bell System that were abandoned in the antitrust settlement: complete integration of universal-access, local service with universal long distance service; complete compatibility throughout the system under unified central control; and, finally, integration of research on all levels, from pure science to product design and operational application. It was precisely because the antitrust suit challenged these features of the Bell System that the Pentagon strongly protested against it. But in the aftermath of Vietnam, nobody listened. What will happen now that the breakup of the Bell System is an accomplished fact? How much compatibility must there be in the nation's telephone system, in telephone receivers, switchboards and central stations, in long distance circuits and long distance service, in the ability to switch automatically from a damaged circuit to another route, so as to support mobilization, the organization of war production, and the transportation of defense materiel, let alone military command in time of war?

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Under the antitrust settlement, defense communications are going to be fragmented. AT&T is bidding on the government's long distance business, but a lot of "discounters," especially MCI, are also trying to get it. So is Bell Atlantic, the regional operating company serving Washington, D.C. There is going to be a host of suppliers offering different kinds of equipment to all government agencies, including the Defense department. And AT&T is altogether forbidden to offer "end to end" services—that is, connections to local telephones—except for a few highly specialized installations at the Department of Defense and the Strategic Air Command.

But surely there is a limit beyond which the fragmentation of our communication system endangers the nation. Pearl Harbor, we now know, happened in large part because a Navy telephone circuit was out of order at the critical time, whilst no interconnection existed to other undamaged circuits. Would we risk similar disaster if we have a number of competing long distance systems rather than one integrated one, and if long distance and local service are separated managerially, technically, and in their equipment?

We may thus soon be faced with the need to re-think the Bell antitrust decision as far as it affects national security. One possibility, and it is being seriously studied in the Pentagon, is for the military to build its own communications system. No one knows how much it would cost, but it would be extremely expensive; one guess is about $100 billion. It would also weaken the civilian telephone system by taking away from it its largest user and the one most willing to try out new technology, and to pay for it.

But there emerged recently, in April 1984, a totally different proposal: to repeal the antitrust settlement with respect to all governmental telecommunications and to turn all of them—local service, long distance, and equipment—back to AT&T. In fact, AT&T has already applied to the Federal Communications Commission for a waiver of the antitrust decree to allow it to submit such a bid to the government. I suspect that the Pentagon will strongly support AT&T; indeed, I suspect that the Pentagon has encouraged AT&T to make this bold move. Whether AT&T's request will be granted is, of course, quite doubtful. There is no precedent in antitrust history for anything so bold and so radical.

AT&T's request would go a long way towards nullifying the antitrust decree's central feature: the absolute separation of long distance from local service. And it would do so with respect to the country's largest single telephone user, the federal government, with a total telephone bill of nearly $2 billion. Above all, what

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AT&T is asking is for the government to admit, at least implicitly, that the breakup of the Bell System was a major and potentially disastrous mistake. Not only will all other providers of telephone service—former Bell operating companies, as well as all long distance discounters and equipment manufacturers other than Western Electric—fight AT&T's request, but within the government and in the Congress there will also be enormous opposition.

Still, it might be the only solution. And if AT&T's request for a waiver is not granted, we will sooner or later have to tackle the question of defense communications—and probably sooner. Some thoughtful people I know in the military, who are by no means alarmists, think the question might come up well before the end of the next presidential term.

The achievements—and problems—of regulated monopolies

The AT&T suit was by far the biggest antitrust action ever taken, and not only because AT&T was the country's biggest nongovernmental enterprise. It also had far more dramatic results than any previous antitrust suit ever aimed at or achieved. What, then, are its lessons for regulation and for antitrust—two pivotal American institutions—both, by the way, almost exact contemporaries of the Bell Telephone System?

The regulated monopoly was one of America's most innovative and most successful contributions to the art of government. In one simple concept it solved what had seemed an insoluble dilemma: either to leave a "natural monopoly" to "free enterprise" and thereby give it a license to extort, or to nationalize it and thereby condemn it to almost certain bureaucratic arrogance, high costs and inefficiency. Without exception, America's regulated monopolies have given better service and have done better than nationalized counterparts in the rest of the developed world. The Bell Telephone System was, of course, the premier example, giving the country the world's finest telephone service at rates up to 50 percent below those of any other industrialized country. American electric utility costs, too, are almost everywhere lower than those of electric utilities elsewhere with comparable energy sources (for example, coal, oil, or water power).

But even a "regulated monopoly" can become dysfunctional. As soon as there is any competition, as soon as there is an alternative way of producing the same consumer satisfaction or of filling the same consumer want, regulation becomes counterproductive. It no longer "regulates" but it still forbids and stifles. It can no longer

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protect its industry and maintain its monopoly. But it can, and will, make it difficult for its industry to compete, to modernize itself, to meet the new threat. Yet there is no mechanism for abolishing outmoded regulation.

What then happens is messy, capricious, expensive, and bound to hurt a good many people, innocent bystanders included. The outcome is unpredictable and quite unlikely to be what is most rational and most in the national interest. In some cases we have left things to blind chance. One example is what is now happening in financial services. It bears not the slightest resemblance to what anyone would have foreseen or advocated when it first became apparent 20 years ago that our financial rules, demarcation lines, and regulations would rapidly become obsolete and meaningless. But with respect to the railroads, the outcome—equally left to chance—is quite different. What is now emerging, after 30 years of turmoil—and without the repeal of a single ordinance, rule, or regulation, is a system of five or so major national, if not transcontinental, railroads. That is almost exactly what a long-dead ICC Commissioner, Joseph Eastman, proposed almost 60 years ago when it first became apparent that cars and trucks were nibbling away at the railroad's monopoly on land transportation. Other industries—airlines and trucking, for instance—have been "deregulated" with the major result of forcing their workers' wages down. And with respect to the telephone, we used an antitrust suit with results that no one can foresee as yet, but which almost certainly will not be what anyone—Bell System executive, antitrust lawyer, or disinterested outsider—would have foreseen, planned for, or aimed at.

Is there a better method? The answer is probably "no." An old idea, a "sunset law" under which regulatory statutes expire every so often and have to be re-enacted—say, every 30 years—is most unlikely to work. Every regulation creates its own constituencies. Regulation has to be undermined *de facto*; *de jure* it is likely to continue long after the reality of regulated monopoly has disappeared, whether through the emergence of cars and trucks, through that of charter planes, through Citicorp becoming in effect a truly "national" bank, or through discounters offering long distance telephone service at cut rates. Indeed, the one probable result of "sunset laws" is to tighten regulation just when economic and technological reality abolishes the "natural monopoly." The only consolation may be that liquidating an obsolescent government monopoly is likely to be even messier, costlier, less predictable. (Witness the vicissitudes of the U.S. Post Office, beset on one side by electronic mail and on the

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other by private express services. Or examine the Japanese National Railroads, which are not allowed to do anything at all by their political and trade-union bosses, but which have already lost all their freight traffic and are now rapidly losing their passenger traffic as well, while unsubsidized private railroads paralleling the tracks of the national system run full trains to the same destinations, charge half the fare the national system charges, and make money into the bargain!)

Antitrust moralism

Antitrust, too, was an American contribution to the art of government, but a far more debatable one. It may come as a surprise to laymen to learn that most American economists have never had much to say for the antitrust laws. They consider such laws morality rather than economics. One reason is that economists, by and large, are not terribly frightened by non-governmental, that is, business monopolies. Ever since a German economist, Robert Liefmann, published his comprehensive study of business monopolies (*Die Kartelle*) in 1906, economists have known that business (that is, non-governmental) monopolies are short-lived. All they do, as a rule, is provide an umbrella of high prices under which competitors then grow fast and risklessly. Thus, Rockefeller's Standard Oil Trust held an umbrella of high prices over the newcomers—Texaco, Gulf, Shell—80 years ago. And the Bell System held an umbrella of high long distance rates over such discounters as MCI and Sprint. The only exceptions are what Joseph Schumpeter (1883-1950) called "intelligent monopolists," that is, monopolies that maintain their leadership position by cutting their own prices before competition does, and faster than competition can do it, and which themselves make their products obsolete before the competition does. Schumpeter's example was the Bell Telephone System—and that was, of course, the foundation for Bell's strength until it ran into the inflation of the late 1960s and 1970s. Another example would be IBM today. "Intelligent monopolies" may indeed last a long time, but of course the "intelligent monopoly" uses its economic power to benefit the consumer rather than to extort from him.

There is an even more important reason, however, for the jaundiced view most American economists take of antitrust: They see no results. Or rather they see only wrong results which are almost the opposite of what antitrust promises. In terms of concentration of economic power, the American economy, despite antitrust, differs very little—and certainly not in statistically significant magnitudes—

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from any other economy in a similar stage of development, even though most of these others have had no antitrust laws and have certainly not enforced those they have had. Indeed, it is pretty obvious that concentration is determined by technology and market forces rather than by law, and is pretty much the same in the same industries across all boundaries. But as a result of antitrust, economic concentration and combination in this country have taken peculiar forms, and not necessarily the most benign ones. Antitrust has enormously encouraged mergers. For under the antitrust laws, units within the same legal entity are considered "one business" and are basically exempt from antitrust with respect to their dealing with one another. In other countries, however, there is the "group" rather than the merger. In the "group," the individual units maintain their independence and indentity though tied to each other through stock holdings (usually minority holdings, by the way). Antitrust would, however, consider the "group," composed as it is of independent legal entities, a clear violation; as a result, antitrust has greatly favored the disappearance of autonomous, self-governing and smaller enterprises in favor of the behemoth. And then because antitrust frowns on concentrations of economic power in the same markets, it has virtually forced American companies to grow by forming "conglomerates" without organic or business unity (for example, ITT's telephone equipment businesses adding to themselves a bakery and an insurance company). Few economists would consider the "merger" preferable to the "group," or the "conglomerate" preferable to either.

This will not, of course, impress antitrusters in the least. That economic concentration in this country, despite its antitrust laws, is no lower than among the "heathen" proves only two things: the antitrust laws have to be enforced much more strictly, and the Evil is even more powerful, more wicked, and more devious than anyone could imagine. To economists, laws like antitrust are hygiene. To the true antitrust believer, they are morality. And morality—at least in the United States—always has a great deal more appeal than something so pedestrian as hygiene. Most American economists would agree that even repealing the antitrust laws in their entirety, let alone their "monopoly" provisions, would not cause great harm to the American economy. The offenses that need to be forbidden —price fixing, discriminatory pricing, discriminatory rebates—are adequately covered by common law, after all, and are adequately dealt with in countries that are totally innocent of antitrust legislation. Still, antitrust is sacred. A proposal to repeal the bans on "con-

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centration" and "monopoly" would have about as much chance of success as a proposal to close all law schools for the next 30 years.

The social costs of antitrust

But still, the AT&T suit has shown that some reforms should at least be seriously considered. The first one might be to introduce into antitrust the overwhelming consensus among American economists as to what is "analysis" and what is "policy." "All economists," an oft-quoted saying goes, "agree that the only purpose of economic activity and its touchstone is the consumer. Anyone who believes that the purpose is anything else (employment, for example) is not an economist." Not quite true, but it will do.[2]

For the great majority of American economists, and of economists anywhere, this only applies to *economic analysis* and not to *economic policy*. But for a tiny minority—George Stigler in Chicago and his disciples—it applies to both. To some considerable extent their influence has been wholesome. Stigler's insistence that in economic analysis nothing else be considered but strictly economic factors is a badly needed antidote to the sloppiness that prevails in arguments about economic policy. It is indeed highly desirable, as Stigler has demanded for years, that policy makers start out with the knowledge of the purely economic facts so that they face up to the costs of any deviation therefrom in the policy they then choose.

But his disciples go much further. They demand that no deviation from the pure economic analysis be allowed in *deciding* on economic policy.[3] And Stigler's disciples control antitrust. To consider anything else—impact on foreign policy or on defense, social consequences, anything—is "impure" if not prostitution. For the antitrust economist, the benefit to an abstract "consumer" is the only consideration. The Chicago economists, for instance, refused to accept as relevant the argument that a Bell System breakup would inevitably mean higher rates for the poor and lower rates for busi-

[2] An important minority has held for nearly 200 years that the purpose is production rather than consumption, and economic development rather than equilibrium. In origin this is *American* economic theory, indeed, the only major important economic theory ever to come out of the U.S. It was first formulated by Alexander Hamilton, then taken up by Henry Clay as the "American System." Friedrich List took it from America to Germany in the 1830s, where it became the foundation for Germany's industrial development into a major economic power. The one major contemporary economist who adhered to it was Joseph Schumpeter (1883-1950). The most consistent practitioners today are, of course, the Japanese.

[3] The best presentations of this point of view are the papers of the Chicago economists who prepared the AT&T antitrust suit for the Justice Department. They are collected in *Breaking Up Bell: Essays in Industrial Organisation and Regulation*, edited by David S. Evans. (New York: North Holland, 1983).

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ness; the only thing they allowed was the total impact on all consumers, that is, the total national telephone bill. For, as the group argues, any concession, any deviation is the first step down the slippery slope. It is "playing politics with the law." To the great majority of American economists, this is virtue carried to the point of madness.

For antitrust *is* politics. The Reagan administration declared last winter, in connection with an antitrust ban on a proposed merger between two very large steel companies, that "it does not allow politics to enter antitrust; it is entirely a matter of the law." This is sanctimonious twaddle, and disingenuous to boot. A major antitrust suit is, of necessity, a highly political matter—and the way it is settled even more so. The suit against AT&T, for instance, would hardly have been brought had inflation not eroded the company's political support to the point at which it became politically vulnerable. And the whole point of the steel merger decision was political: whether it is politically preferable to allow major steel companies to merge rather than to impose import restrictions on steel from Europe and thereby to risk a trade war with the Common Market. And, indeed, no sooner had the White House officially declared that it had nothing to do with the steel-mergers case than antitrust reversed itself and allowed the merger. It is simply not true, as the antitrust economists maintain, that there exists no reasonably rigorous and objective theory to consider extra-economic factors in an economic-policy decision. That theory has been in existence for 50 years now, in the "welfare economics" of Arthur Cecil Pigou. What "welfare economics" does is determine, with considerable precision, the economic costs of "trade-offs" from the purely economic, purely consumer-focused result of economic analysis. How much would it mean in additional costs if, for example, long distance rates were maintained at a higher than strictly economic level to provide subsidies for minimum local service? How much would it cost in economic terms to make this or that social or political concession? What, in other words, are the *economic* costs of a given policy? Policy, by definition, can never be just one thing—that is, social or economic or military—it always has many dimensions. Who loses, who benefits, and by how much?

But the antitrust economists are quite right: The answers to these questions are not really to be found in the law any more than are the settlement terms for an antitrust decree. What is therefore needed (and, by the way, most judges would agree) is to divorce analysis from policy in major antitrust suits as we routinely do in so many

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other areas. Legal and economic analysis should govern until a company or an industry is found in violation. But then a panel of high-level experts—maybe one nominated by the prosecution, one nominated by the defense, one a public member (or a panel appointed by the Council of Economic Advisors)—would work on the "trade-offs," the "welfare economics." The panel should probably be limited in its considerations to a fairly small number of issues: major social impact; major economic impacts such as those on productivity, capital formation, and employment; the impact on America's competitive position in the world economy and on America's technological leadership; the impact on national security. In the AT&T case, such a panel would surely have recommended continuing financial support of the Bell Labs by the operating companies. And it might also have forced us to face the problem of defense communications. The panel should advise rather than arbitrate, the judge making the final decision. But the judge needs advice; nothing in a judge's background or career qualifies him in these matters. They are also matters which can only be mismanaged if handled in adversary proceedings.

Of course any such reform, or anything even remotely like it, is in the future. But it may not be a very distant future. If the Bell breakup works out and if ten years hence the U.S. still has telecommunications leadership, well and good. But if, as is quite likely, the ten years after the antitrust liquidation of AT&T's "natural monopoly" bring more gadgets but otherwise only increased costs, damaged technological leadership, and compromised national security, we may then be ready to reconsider.

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The rich, the poor, and the taxes they pay: an update

JOSEPH A. PECHMAN & MARK J. MAZUR

FIFTEEN YEARS AGO, an article by Joseph A. Pechman entitled "The Rich, the Poor, and the Taxes They Pay" was published in this journal. Then, as now, the distribution of income was a hotly debated subject. Relying primarily on introspection and casual investigations, people are forever arguing whether the rich or the poor are getting richer. Such arguments cannot be resolved without hard facts, however. Income inequality is a serious issue and those who make policy decisions on the basis of intuition or dogma can do considerable damage.

The earlier article, which examined data for the period 1952-1967, attempted to bring some coherence into the income distribution controversy. We can now add data for an additional 14 years and thus are able to examine what happened to the U.S. income profile over the last three decades.

The basic factors of production are land, labor, and capital, and all income people receive can be traced back to the ownership or use of one or more of these. Every society has attempted to modify the distribution of income generated through the workings of market forces, and in most Western countries such attempts take the form of tax and transfer programs. (Regulatory policies also have impor-

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tant distributional effects, but such policies are usually adopted for reasons other than to change the distribution by income classes.)

A key to addressing the issue of income inequality is the idea of taxing people according to their ability to pay: Those with higher incomes should pay higher taxes, since they have the wherewithal to do so. In practice, this idea translates into a scheme of progressive taxes.[1] The federal income tax is often considered quite progressive, with statutory rates going from zero on taxable incomes less than $3,400 for married persons filing joint returns ($2,300 for single people), to 50 percent for incomes above $162,400 ($81,800 for single people). While it is often assumed that such rates must have a significant impact, there are many ways to escape these rates, and the overall effect of the tax system on the income distribution has been small (see below).

A more powerful distributional tool is the system of transfer payments, which is designed to help those who do not earn enough from the market system to make ends meet (welfare), to cushion declines in earnings resulting from unemployment, retirement, and disability (social security), and to provide medical care to low-income persons and the aged (medicaid and medicare). Thirty years ago, transfer payments added 3 percent to personal incomes in the United States; today, the figure is close to 14 percent. While in the United States most of these programs are not means tested, it turns out that transfer payments do have a significant equalizing effect on the distribution of income.

Although many people think of "the rich" as a class to which only a few belong, psychologists have long noted that people with money perceive themselves as being relatively worse off then they are. Therefore, it is useful to indicate what income figures attach to various percentiles in the income distribution. For the year 1981, the top 1 percent of family units in the United States was made up of those whose income (including realized capital gains and excluding transfers) was above $91,000. Further, a family was in the top 2 percent with an income above $70,800, the top 5 percent with an income over $49,200, the top 10 percent with income over $39,400, and the top 15 percent of the income distribution with income above $34,600. Most of the readers of this article, then, are among the rich

[1] Since the terms are often used loosely, it's a good idea to define what is meant by progressive, regressive, and proportional taxes. Taxes are *progressive* if they increase as a percentage of a person's income as income rises, *regressive* if they decrease as a percentage of income as income rises, and *proportional* if they are the same percentage of income in all income classes.

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and super-rich, though it is likely they would quarrel with this designation.[2]

The distribution of income before taxes

As surprising as it may seem, the U.S. government does not publish official estimates of the distribution of income. Several sources of data exist, though, that provide interesting insights into income profiles, if these sources are properly combined. This article makes use of two major bodies of government data: the annual *Statistics of Individual Income*, published by the Internal Revenue Service, and the *Current Population Reports* of the U.S. Census Bureau. Both sources have their weaknesses. The Census Bureau surveys a sample of households every year, but these surveys systematically understate income, particularly in the highest brackets. On the other hand, the tax return data produced by the IRS do not include the incomes of those who are not required to file returns. For the income distributions presented below, tax data were used since we are particularly interested in the high income units. The total number of family units is based on Census data, and estimates of total income (as defined in the tax code) were obtained from the Bureau of Economic Analysis of the Department of Commerce.

For historical completeness, a brief examination of the income distribution data for the pre-1950 period is warranted. By all accounts, a significant change in the pre-tax distribution of income occurred during the Depression and World War II. The experts seem to agree that the income distribution became more equal for two reasons: Business and property incomes suffered a severe decline during the 1930s, and earnings differentials between low-skilled and higher skilled workers were narrowed when employment increased during the war. The most authoritative estimates, prepared by Selma Goldsmith and her associates, suggest that the share of income received by the top 5 percent of the nation's consumer units (families and unrelated individuals) declined from 30 percent in 1929 to 26.5 percent in 1936 and 20.7 percent in 1944. Correspondingly, the share received by the top 20 percent went from 54.4 percent in 1929 to 51.7 percent and 45.8 percent in 1936 and 1944, respectively. To see what happened to these trends after the war, we shift to the data from postwar tax returns.

[2] These estimates are based on tax data. Taxpaying units do not correspond exactly to family units because children and other family members may file separate returns if they have income. We assume that the top 15 percent of the nation's tax units are similar to the census family units and that the cases that differ represent roughly the same percentage of total units each year.

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Table I presents the shares of national income received by various categories of the top 15 percent of tax units. The shares received by the richest taxpayers (say, those in the top 5 percent) have remained remarkably constant over the last three decades. What this means is that these persons have not enjoyed larger increases in income than the average family unit. However, a shift occurred among those who are not quite as well off. Specifically, those in the 6th to 15th percentiles of the income distribution increased their share of the nation's product from 14 percent in 1952 to 16 percent in 1967 and to 18 percent in 1981. Since the top 5 percent of taxpayers had a relatively constant share of income over the period, this gain came at the expense of the lower 85 percent of the income distribution.

Table I. Before-Tax Income Shares, Tax Data

	Top 1% of Tax Units	*Top 2% of Tax Units*	*Top 5% of Tax Units*	*Top 10% of Tax Units*	*Top 15% of Tax Units*
1952	9%	12%	19%	27%	33%
1963	8%	12%	19%	28%	35%
1967	9%	13%	20%	29%	36%
1972	8%	12%	20%	29%	37%
1977	8%	12%	20%	30%	38%
1981	8%	12%	20%	30%	38%

Briefly, then, the so-called "middle income" classes improved their relative before-tax income status over the past 30 years. These classes consist of many of the professionals in this country (doctors, lawyers, engineers, accountants, business school professors, middle and upper level management, etc.), as well as the highest paid members of the skilled labor force. These taxpayers may not realize how fortunate they are; indeed, they are quite likely to consider themselves as barely keeping up. In the aggregate, this is clearly not true; our data show that the middle income classes have done much better than most.

The effect of taxes

Of course, the distribution of incomes generated in the marketplace is only part of the story. The effect of taxes and transfers on the income distribution needs to be considered to determine how governmental programs affected the income shares received by the various income groups.

Since one of the objectives of federal income taxation is to tax according to ability to pay, it is worthwhile to ask whether this objec-

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tive is being realized. To answer this question, we look first at effective rates of the federal income tax in the various income classes, and then at the distribution of income after this tax is paid. The federal income tax being the most progressive element of the tax system, the distribution of income left after this tax is paid exaggerates the influence of taxes on income inequality.

Before looking at the data, it may be helpful to review some of the changes in the federal income tax during the past half century. Tax rates rose to a peak during World War II, when top rates exceeded 90 percent and personal exemptions were sharply reduced to raise the necessary wartime revenue. Those in the lowest income bracket were subject to a tax of 23 percent (in 1944). Immediately after the war, rates declined, only to be raised again during the Korean War. Starting in 1964, Congress began lowering the income tax rates, pausing only in the late 1960s for a temporary surcharge imposed to finance the Vietnam War. This surcharge lapsed in 1970, and rates remained constant until 1981, when the top rate was reduced from 70 percent to 69.125 percent and the lowest bracket rate was reduced from 14 percent to 13.825 percent (effective in 1984). When the Reagan tax cuts became fully effective at the beginning of 1984, the top rate had been reduced further to 50 percent and the bottom rate to 12 percent. Thus, the recent trend in the nominal tax rates is one of reasonably steady decline.[3]

At the same time, people have rightly complained about being pushed into higher and higher tax brackets by the combination of both real income growth and inflation. In the past, Congress reacted to this "bracket creep" by periodically reducing statutory rates and increasing personal exemptions; in 1981 it indexed the tax rate brackets and the exemptions automatically for changes in the general level of prices beginning in 1985. Simple comparisons of statutory tax rates are misleading where nominal, rather than inflation-adjusted, incomes are taxed during a period of high inflation (such as the past 15 years in the United States).

Table II, which provides a series on the average tax rates paid by various groups of taxpayers, reveals the extent to which bracket creep has increased the effective tax rates of those at the top of the income distribution. Four important points may be noted: First, the effective rates decline as one moves down the income distribution from the highest incomes, showing the effect of progressive rates;[4]

[3] Over this same period, personal exemptions were increased gradually. These went from $500 in 1944 to $600 in 1948, $750 in 1972, and the current $1,000 in 1979.

[4] Of course, these are aggregate figures and thus conceal wide variations in average tax rates paid by different families in each income class.

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second, effective tax rates declined steadily from 1952-1972; third, the decline in effective rates was reversed during the past ten years as bracket creep reached significant proportions; and, finally, the burden imposed on taxpayers by bracket creep was much larger for those in the 11th to 15th percentiles of the income distribution (more than a 20 percent increase in average effective rates between 1972 and 1981) than for those in, say, the top percentile of the income distribution (approximately a 10 percent increase in effective rates over the same period). Although more recent data are not available, it seems likely that the tax rate reductions made in the Economic Recovery Tax Act of 1981 reversed the effect of bracket creep and probably restored the effective tax rates of the taxpayers considered here to the levels of the mid-1970s.

Table II. Effective Federal Tax Rates on Total Income

	Top 1% of Tax Units	*Next 1% of Tax Units*	*Next 3% of Tax Units*	*Next 5% of Tax Units*	*Next 5% of Tax Units*
1952	33%	20%	16%	14%	12%
1963	27%	20%	16%	14%	13%
1967	26%	18%	15%	13%	12%
1972	27%	19%	16%	14%	13%
1977	31%	22%	18%	16%	14%
1981	30%	23%	21%	18%	16%

It is a fairly simple matter to deduct the tax paid by each of the income groups from their before-tax incomes to obtain a distribution of disposable income. These results, shown in Table III, modify only slightly the conclusions derived from the before-tax distributions. The shares of after-tax income received by the top 3 percent remain amazingly stable, but those received by the next 12 percent, the "middle income classes," increase substantially (from 20 to 25 percent), over the period 1952-81. This increase parallels the one noted in the before-tax income shares.

Table III. After-Tax Income Shares

	Top 1% of Tax Units	*Top 2% of Tax Units*	*Top 5% of Tax Units*	*Top 10% of Tax Units*	*Top 15% of Tax Units*
1952	7%	10%	16%	24%	30%
1963	7%	10%	17%	26%	33%
1967	7%	11%	17%	26%	34%
1972	7%	10%	17%	27%	35%
1977	6%	10%	17%	27%	35%
1981	7%	10%	17%	27%	35%

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One may conclude, then, that the federal income tax reduces the inequality in the overall distribution to a modest degree (compare the before-tax and after-tax shares). This reduction became less pronounced between 1952 and 1972, but more pronounced during the period of bracket creep thereafter. As effective tax rates declined in the earlier period, the share of the top taxpayers in disposable income either remained the same or increased despite the constancy of the before-tax income shares. Since 1972, their disposable income shares remained the same, even though their before-tax-increase shares increased. Bracket creep seems to have been the instrument by which the increasing inequality of before-tax income was moderated.

The effect of transfer payments

The other major element of government policy affecting the distribution of income is the system of transfer payments. As mentioned earlier, this system includes programs of public assistance that are designed explicitly to help the poor as well as others not designed primarily for this purpose (for example, unemployment and retirement benefits). While the effects of transfer programs on the distribution of income cannot be measured exactly, the Brookings Institution has run computer simulations of the tax and transfer system in the United States for a number of years. Table IV presents the set generated for the year 1980.

It should be noted that, for several reasons, these data are not directly comparable with those presented earlier. First, the income definition used in Table IV includes several sources of economic income that are not taxable (for example, imputed rent on owner occupied housing, unrealized appreciation of capital assets, and pension fund accumulations). Second, total taxes consist of *all* taxes levied by federal, state, and local governments. They include sales and excise taxes, property taxes, corporation income taxes, and state and local income taxes, in addition to the federal income tax levied on individuals. Third, percentile groupings of family units are used, rather than tax units.

Table IV makes obvious the relatively mild degree of progressivity of the tax system and the highly progressive nature of the transfer system. Taxes go from 23 percent of income in the second decile to 29 percent in the top decile.[5] Transfer payments, on the

[5] The decline in the effective tax rate from 42 percent in the first decile to 23 percent in the second is an artifact of annual accounting. People who have temporarily low incomes spend more than their incomes and therefore appear to be taxed more heavily. If the figures were available for a longer period, this effect would be reduced

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Table IV. Taxes and Transfers as Percent of Income, 1980

Family Income Percentiles[a]	*As Percent of Income:*		
	Taxes[b]	*Transfers*	*Taxes less Transfers*
0-10	42%	158%	−116%
10-20	23%	58%	−35%
20-30	24%	35%	−11%
30-40	25%	24%	1%
40-50	26%	15%	11%
50-60	26%	11%	15%
60-70	26%	8%	18%
70-80	27%	6%	21%
80-90	28%	4%	24%
90-100	29%	3%	26%
All families	27%	10%	17%

[a] Income includes wages and salaries, fringe benefits, interest, dividends, rents, entrepreneurial incomes, and retained corporate earnings, but excludes transfer payments.

[b] Assumes that the corporation income and property taxes are borne by owners of capital and payroll taxes are borne by workers. The individual income tax is assumed to be paid by the taxpayer and sales and excise taxes are assumed to be paid by the consumers of the taxed items.

other hand, fall dramatically as incomes rise—from almost 160 percent of income in the lowest decile to 3 percent in the highest.[6]

Clearly, redistributing income in this fashion moderates income inequality more by increasing resources available to those at the base of the income pyramid than by taking away more in taxes at the top. The result, however, is that the income moderation achieved by the combined tax-transfer system is quite substantial. The last column of Table IV bears this out. Negative numbers in this column indicate that the families receive more in transfer payments than they pay in taxes of all types; positive figures indicate that they pay more in taxes. On balance, families in the lowest three deciles receive more transfers than they pay in taxes, while those in the top seven deciles pay more taxes than they receive in transfers. The tax-transfer system is, therefore, highly progressive.

or wiped out. The assumptions used (see footnote b, Table IV) to distribute taxes by income classes are those generally supported by modern tax economists. Alternative assumptions (e.g. that the corporate tax is passed on to the consumer) would make the tax system less progressive or even regressive.

[6] The progressivity of the tax system may be understated in Table IV because the payroll taxes levied to support social security retirement and disability benefits are regressive, but the benefits are progressive. On a lifetime basis, if taxes and transfers were netted out for the same individuals, the tax system itself would appear to be more progressive. However, the progressivity of the tax-transfer system as a whole (shown in the last column of Table IV) is not greatly affected by the separation of taxes and transfers.

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More (net) equality

On the basis of the data presented here we may draw several conclusions:

1. The market distribution of income has become more unequal over the past three decades. Thus, the share of society's product accruing to the top 15 percent of families has increased steadily over this period.

2. The federal income tax is only mildly progressive and has not moderated income inequality to a significant degree. The income distribution after the payment of federal income taxes is more equal than before, but only slightly.

3. The system of transfer payments, which has grown rapidly over the past 30 years, is highly progressive. Even though many of its components are not "means tested," it does have a big moderating effect on income inequality.

4. The distribution of income after all taxes and transfers is more equal than the distribution before taxes and transfers. Since transfers rose rapidly between 1952 and 1980, the inequality in the distribution of income after taxes and transfers must have been greatly reduced. This growth in equality may have been reversed by the Reagan budget and tax cuts beginning in 1981, but the figures to measure the extent of the reversal will not be available for some time.

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The hidden prosperity of the 1970s

CHRISTOPHER JENCKS

BY NOW almost everyone knows that the long economic boom which began after World War II petered out in the early 1970s. Inflation accelerated, unemployment rose, productivity stagnated, and after adjusting for inflation, real wages fell. As a result, Americans had to run hard just to stand still, and the dream of a steadily rising standard of living evaporated.

The most widely cited evidence for this view is probably the Census Bureau's annual report on trends in family income. This report, published every year since 1948, always begins by comparing the change in median family income during the previous year to the change in the Consumer Price Index. This comparison shows that "real" family income, which had risen 38 percent during the 1950s and 34 percent during the 1960s, rose only 0.4 percent during the 1970s.

Such statistics have been widely cited in political debate. Conservatives have invoked them to show that we can no longer afford the luxury of a large welfare state or policies aimed at economic redistribution, and that increased government intervention in the economy during the 1960s and 1970s had a negative effect on subsequent economic growth. Liberals and radicals have invoked pre-

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cisely the same statistics to show that the private economy is being mismanaged and that we need a government-sponsored "industrial policy," patterned on Japanese and European experience, to promote economic growth. At a more mundane level, such statistics reinforced Ronald Reagan's 1980 claim that those who had held political power during the 1970s had mismanaged the economy, and that we needed "new leadership" with a "new approach" if we were to do better in the future.

But Census statistics on family income do not describe what happened to the American standard of living during the 1970s at all accurately. Whereas Census statistics imply that the standard of living stagnated during the 1970s, more direct measures of material well-being often showed marked improvement, and some showed as much improvement during the 1970s as during the supposedly more affluent 1950s and 1960s. This does not mean that the economy as a whole was healthy during the 1970s. It was not. But despite high inflation and high unemployment, the average American family was better off in 1980 than in 1970. To demonstrate this I will focus on four areas: health, housing, transportation, and food consumption. In each case I will compare changes during the 1970s to changes during the 1950s and 1960s. After looking at changes in these four areas I will turn to the question of why family income statistics for the 1970s are so misleading. I will conclude with a brief discussion of the early 1980s.

Health

Life expectancy is the most widely used measure of a nation's health. Estimates of life expectancy tell us how long people could expect to live if current death rates were to prevail in the future. Table I shows that life expectancy rose steadily from 1950 to 1980, but that the increase during the 1970s was much larger than during the 1950s or 1960s. Indeed, life expectancy rose more during the 1970s than during the 1950s and 1960s combined.

Table I. Changes in Life Expectancy and Infant Mortality[a]

	1950	*1960*	*1970*	*1980*
Life Expectancy at birth (in years)	68.2	69.7	70.9	73.7
Infant Mortality per 100,000 births	29.2	26.0	20.0	12.8
Expenditure per Person on Medical Services in "Constant" Dollars	$374	$460	$731	$1024

[a] *Source:* Derived from *Statistical Abstract of the United States* (*SAUS*), 1983-1984.

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Rising life expectancy during the 1970s was not the result of any single medical breakthrough, like antibiotics in the 1940s. Death rates fell for a wide range of diseases, and in all age groups. The fact that fewer people died from heart disease was the most important single reason for the overall increase in life expectancy, but there were also fewer deaths from many other causes, ranging from pneumonia to accidents. Mortality rates declined most among those groups where they had traditionally been highest. Among nonwhites, for example, life expectancy rose from 65.3 to 69.5 years. Among whites, it rose only two thirds as much, from 71.7 to 74.4 years.

Another widely cited index of a nation's health is infant mortality, which includes deaths during the first 12 months after birth. Like life expectancy, infant mortality improved more during the 1970s than it had during the 1950s or 1960s. Indeed, the decline in infant mortality accounted for almost a fifth of the overall increase in life expectancy during the 1970s. Both the white and nonwhite infant mortality rates declined by a third, but since the nonwhite rate was almost double the white rate in 1970, the absolute decline was much larger for nonwhites than for whites.

Table I also shows the monetary value of medical services from 1950 to 1980, corrected for inflation in medical prices. While life expectancy rose fastest during the 1970s, the monetary value of medical services rose as much in the 1960s as in the 1970s. As we shall see, such expenditure figures mean relatively little, because they ignore the value of "free" improvements in medical care that derive from increased medical knowledge and better medical practice. Trends in health depend as much on "technical" innovations of this kind as on the tangible resources devoted to medical care.

Housing

The median price of a new single-family home rose from $23,400 in 1970 to $64,600 in 1980, and mortgage rates rose from 8.5 percent to 12.7 percent. Other things being equal this meant that the monthly mortgage payment on a new house more than quadrupled. Family income rose at only half this rate, so the burden of financing a new home doubled. According to conventional wisdom this put home ownership beyond the reach of most families.

Such statistics tell only part of the story, however. While interest rates rose during the 1970s, inflation rose even faster, so that the "real" interest rate (nominal interest minus inflation) became negative. As a result, those who bought a house could expect its value to increase more in most years than they paid out for interest on their

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mortgage. For all practical purposes, therefore, interest payments on residential mortgages became a form of saving. Such payments were a particularly attractive form of saving, because they were tax deductible. And when owners chose to convert such savings to cash by selling their homes, the profits were subject to extraordinarily favorable tax treatment. As a result, the true cost of home ownership was far lower than the nominal cost. Indeed, for many home owners the true cost of home ownership, even after allowing for maintenance and depreciation, was probably negative during the 1970s.

While home ownership looked like an increasingly attractive investment during the 1970s, other investments looked worse and worse. Savings accounts paid artificially low interest rates, and even money market accounts paid less than inflation. Both were fully taxable. The stock market, which had traditionally been advertised as a hedge against inflation, failed dismally in its appointed role. Stock prices were almost the only prices that refused to rise during the 1970s. For a family with savings, therefore, home ownership was by far the best available investment. The results were predictable. Personal savings flowed out of stocks, bonds, and savings accounts into residential real estate. Everyone with surplus cash bought his own home, including apartment dwellers who had rented all their lives. As a result, 64.4 percent of all American households owned their own homes in 1980, compared to 62.9 percent in 1970. This increase was not as large as during the 1950s, when home ownership rose from 55.0 to 61.9 percent, but it was larger than during the 1960s, when ownership only rose from 61.9 to 62.9 percent.

While home ownership became more widespread during the 1970s, it was increasingly confined to affluent families. Until the 1970s much of the urban middle class had rented apartments, while a lot of poorer rural families had owned their own homes. But as down payments and monthly costs rose, only families that were willing and able to save a substantial fraction of their current income could afford to enter the housing market. And as the profits available in this market rose, everyone who *could* afford to enter the market did so. As a result, home ownership became increasingly correlated with income. In 1970 home owners' median income had been only 53 percent higher than that of renters. By 1980 the difference was 89 percent.

While home ownership is an important political symbol, renters often live better than owners with comparable incomes. As a result, trends in home ownership do not necessarily tell us much about housing conditions. Table II summarizes the most widely used mea-

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Table II. Changes in Housing Conditions[a]

	1960	*1970*	*1980*
Median Number of Rooms			
Per Unit	4.9	5.0	5.1
Per Person	1.7	1.8	2.1
Percent of Units Built within:			
Past 10 Years	28	25	26
Past 20 Years	42	46	46
Percent of Units with:			
Television	87	95	98
Complete Plumbing	87	94	97
Telephone	79	87	93
Electric Clothes Washer	55	62	77
Clothes Dryer (gas or electric)	20	44	62
Air Conditioning	12	37	55
Dishwasher	7	27	43
Color Television	0.3	21	63
Monthly Rental Value (in 1980 dollars)			
Per Household	$167	$222	$275
Per Person	49	69	97

[a] *Source:* Derived from *SAUS 1983-1984* and *Economic Report of the President (ERP) 1984.*

sures of such conditions. It omits 1950 because data for that year were not readily available.

The typical American home had 4.9 rooms in 1960, 5.0 rooms in 1970, and 5.1 rooms in 1980. Taken at face value these figures suggest that crowding declined (or spaciousness increased) by the same amount during the 1970s as during the 1960s. But the number of people in the typical household fell more during the 1970s than during the 1960s, so the number of rooms *per person* rose more during the 1970s than during the 1960s. While no historical statistics on room size appear to exist, data on buildings that were still standing in 1981 strongly suggest that square footage rose along with number of rooms.

Of course rooms per person may not be an ideal measure of spaciousness, since there may be some economies of scale in housing. A family only needs one kitchen, for example, regardless of how many members it has. This means that if two adults have two children they seldom feel they need to double the number of rooms in their apartment—though they may feel that they need to move from an apartment to a single family residence with a yard, which may double their housing bill. As this example illustrates, there are no objective standards for determining how much space families of differing size need in order to be equally well-housed. Living with children is different from living with adults no matter how many rooms

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you have, and the same holds for living with another adult instead of living alone. The number of extra rooms you *think* you need when your household gets bigger depends on how the new members of your household behave, how you feel about their behavior, and how many rooms other households of the same size have. Nonetheless, almost everyone would agree that small households need less space than large households. Thus no matter what measure of crowding you adopt, it falls more during the 1970s than during the 1960s.

Ideally, we would also like to have historical data on leaky roofs, unreliable plumbing, broken windows, flaking paint, and so forth, but we do not seem to have them. The age of the housing stock is the most widely used proxy for such problems. America built very little housing during the 1930s and 1940s. To make up for this deficit we built an enormous amount in the 1950s. As a result, an unusually large percentage of all housing was less than ten years old in 1960. This percentage fell during the 1960s and rose during the 1970s. The percentage of units built within the past twenty years, in contrast, rose during the 1960s and was constant during the 1970s. Taken together, the two series suggest little overall change in the age of the housing stock between 1960 and 1980.

If initial standards of construction and subsequent standards of maintenance were as stable as the age of America's housing, the frequency of leaky roofs, defective plumbing, and the like would not have changed much from 1960 to 1980. Popular mythology holds, however, that "they don't build houses the way they used to." No one who has looked at the spread of building codes, or struggled with old galvanized pipes or pre-1939 electrical services, is likely to think that the plumbing and electrical systems of yesterday's houses were initially superior to today's. The main area in which standards show signs of decline is carpentry. My guess, therefore, is that most housing problems were less common in 1980 than in earlier years. In the absence of hard evidence, however, the cautious reader should probably assume that nothing much has changed in this realm.

Household equipment is also important to most families. To give some idea how such equipment has changed over time, Table II shows the percentage of households with television sets, complete plumbing, telephone service, washing machines, dryers, air conditioners, and dishwashers. In evaluating these data the reader should remember that these appliances have a natural "product cycle" that largely determines the rate at which they spread. When a household convenience is first introduced, nobody has had first-hand experience with it, distribution and service networks are thin, and it

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spreads slowly. Once an appreciable number of affluent families have bought a useful item on an experimental basis, however, word about its usefulness spreads, and most families that can easily afford the item acquire it. This is the period of most rapid diffusion. Once all the families that can easily afford the item have it, further diffusion depends on increases in real income, which come relatively slowly. But if economic growth continues, and if the distribution of income remains stable, as it has since World War II in America, almost all families that want an item will eventually get it. At that point further diffusion becomes impossible.

Color television illustrates the early part of the product cycle. Color television was introduced in 1959 but spread relatively slowly during the 1960s. It spread much more rapidly during the 1970s, since by then most stations were broadcasting in color, and color was universally accepted as better than black-and-white. Plumbing and telephones illustrate the last part of the product cycle. Almost all American households had complete plumbing and a telephone by 1970, so these items could not possibly have spread as quickly during the 1970s as they had during the 1960s. Nonetheless, it is reassuring to see that only half as many households lacked complete plumbing and telephone service in 1980 as in 1970. This means that during the 1970s these amenities became standard even in very poor households.

As these examples illustrate, the rate at which a given item spreads in a given decade depends to a great extent on when it was introduced. Clothes dryers, air conditioners, and dishwashers were introduced and spread relatively slowly in the 1950s. They spread faster during the 1960s, when almost everyone who could easily afford them bought them. They spread somewhat slower during the 1970s, since by then their spread required increases in purchasing power as well as increases in consumer acceptance of the product. Clothes washers, in contrast, were already widespread by 1960. If you believe the data in Table II, they spread more rapidly during the 1970s than during the 1960s, implying that the number of families that could afford a clothes washer rose faster during the 1970s than during the 1960s. Since this strikes me as unlikely, I am suspicious of the data, which do not come from a well documented survey.

Since the spread of household conveniences depends so much on when they were introduced, the overall rate of improvement in household hardware also depends to a great extent on when the items you think important were introduced. I selected the items in Table II because they seemed to me to be of unusual symbolic or

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practical importance. I omitted other items of equal cost (e.g. home video recorders) on the grounds that they were less important. It is tempting to argue that such a subjective approach is bound to be idiosyncratic, and that we would do better just to look at changes in expenditure on household conveniences. But the rate of improvement in household hardware is *not* just a function of expenditure. It also depends on what is for sale at any given time. There were more important innovations in household hardware during the 1950s than during the 1960s or 1970s. As a result, useful appliances spread faster during the 1960s than during the 1970s. Video recorders have not changed people's lives to anything like the same extent that, say, air conditioners have, so the fact that people bought video recorders in the 1970s does not imply as much of a change in the standard of living as the fact that they bought air conditioners in earlier decades —and continued to buy them in the 1970s.

The data on household conveniences, crowding, and the age of housing units in Table II suggest that housing conditions, broadly conceived, improved about as much during the 1970s as during the 1960s. As a partial check on this conclusion we can look at the estimated rental value of housing units (including those that were owner-occupied), adjusted for inflation. Rental values do not take account of the value of appliances that tenants ordinarily supply themselves, like telephones and television sets, but they are still instructive. The National Income Accounts indicate that the rental value of the average housing unit rose 24 percent during the 1970s, 33 percent during the 1960s, and 38 percent during the 1950s. If we calculate rental value *per person* instead of *per unit*, the increase was 40 percent in each decade. Such figures confirm the impression that housing conditions improved substantially during the 1970s. The improvement may have been somewhat less than during the 1950s and 1960s, but the difference was certainly modest, and perhaps nonexistent.

Transportation

Private automobiles have been the backbone of the American transportation system since World War II, and access to automobiles has therefore been the main determinant of how easily people can move from one place to another. The best measure of access to automobiles is probably the ratio of registered passenger cars to persons over 16, shown in Table III. This ratio is roughly equivalent to the percentage of potential drivers with a car at their disposal. Table III thus suggests that about 73 percent of adults had a car at their disposal in 1980, compared to 65 percent in 1970.

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Table III. Changes in Auto Transportation[a]

	1950	1960	1970	1980
Passenger Cars per 100 Persons over 16	38.5	52.6	65.1	72.5
Miles per Car		9,500	9,800	8,900
Miles Driven per Person over 16[b]		5,000	6,400	6,500
Median Age of Cars (in years)			5.6	6.6

[a] *Source:* Derived from *SAUS 1983-1984.*
[b] This includes only the mileage of drivers, not passengers.

Table III also shows, however, that people drove the cars at their disposal somewhat less in 1980 than in 1970. As a result, the mean number of miles driven by the average adult remained almost unchanged. If people had more cars but drove the same number of miles in 1980 as in 1970, it seems safe to assume that from the user's point of view the transportation system was somewhat more satisfactory. If, for example, a couple had one car in 1970 which they drove 15,000 miles and had two cars in 1980 which they drove 7,500 miles apiece, they would surely have been better able to go where they wanted, when they wanted, in 1980 than in 1970.

While Table III suggests that adults found it easier to get around in 1980 than in 1970, it also suggests that the improvement during the 1970s was far less than during the 1960s or 1950s. The ratio of cars to adults rose faster during the 1960s than during the 1970s, and mileage per adult also rose substantially during the 1960s. While I do not have mileage statistics for 1950, access to automobiles rose even faster during the 1950s than during the 1960s.

The relatively slow increase in access to automobiles during the 1970s was only partly traceable to budget constraints. While there were still some people who wanted automobiles and did not have them in 1980, the market was approaching saturation. Hardly any household wants more than one car per adult. This means that the ratio of cars to adults is never likely to exceed 100 percent. In practice, there are a lot of people who don't want even one car. Some people are too old, too sick, or too timid to drive. Others, especially in New York City, find it easier to take taxis or public transportation than to cope with endless parking problems. Some urban couples find that one car meets their needs and that a second car is just a nuisance to maintain. Thus even if real income had doubled or tripled during the 1970s, the ratio of cars to adults would probably not have risen above 85 or 90 percent, and it might not even have gone that high.

When we turn from measuring mobility to measuring the comfort in which people traveled, the picture is more complicated. The

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typical American car had less luggage space and less leg room in the back seat in 1980 than in 1970. This was partly because families were smaller, so they needed less room in their cars, and partly because more families had two cars, only one of which had to be large enough for the whole family. But it was also partly because rising fuel costs made drivers more attentive to fuel economy, and hence more willing to sacrifice passenger comfort. How often passengers were actually crowded as a result is anybody's guess.

In most other respects cars became more comfortable during the 1970s. Air conditioning, tinted glass, power windows, power brakes, and stereophonic sound systems were all more common in 1980 than in 1970. The spread of such luxury items makes it hard to believe that people bought smaller cars because they simply could not afford rising fuel costs. Rather, high fuel costs made big trunks and rear seats more expensive than air conditioning, stereo equipment, and the like, and people adjusted their buying habits accordingly. Or perhaps people just became more selfish. Even small cars usually provide ample space for the driver. The costs involved in owning a small car fall mainly on the owner's children and friends, who end up in cramped back seats, sometimes shared with luggage. Air conditioning, tape decks, and power brakes benefit the owner directly. The shift from spaciousness to other forms of comfort may thus reflect changing values as well as changing prices.

Cars also got older during the 1970s. In the 1950s and 1960s many affluent families traded in their car every year or two. By the 1970s this was far less common. Of course trade-ins did not go to the junk yard even in the 1950s and 1960s. Less affluent families bought and drove second-hand cars until the cost of maintaining them exceeded the cost of replacing them, and this remains true today. In assessing the condition of the nation's automobiles we therefore need to focus on their median age, not on the length of time that particular families keep particular cars. But the median age of American passenger cars rose during the 1970s, from 5.6 years in 1970 to 6.6 years in 1980. This was partly because cars were not being driven as far each year, so they lasted longer. In addition, manufacturers began putting more emphasis on minimizing maintenance costs in the 1970s, which may have made cars last longer. I have not been able to find any direct evidence about whether the increasing age of cars meant they spent more time in the garage or broke down more on the road.

All in all, the transportation picture is quite mixed. More adults had a car at their disposal in 1980 than in 1970, but they drove their cars slightly less. Cars were more luxurious in most respects, but they were less spacious. The typical car was older, but we do not

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know if it was less reliable. Overall, the data suggest some improvement in the ease and comfort with which Americans moved about, but not a lot. Automobile transportation certainly did not improve as much during the 1970s as during the 1960s or 1950s.

Food

There is no general agreement about how to measure the quality of what people eat. Nutritional experts evaluate what people eat in terms of its real or imagined medical consequences, while economists ask whether people can afford to eat what they want to eat. The nutritional approach takes no account of how food tastes or of the loss people experience when deprived of things that are bad for them. In addition, the nutritional approach is handicapped by the fact that expert opinion about what people ought to eat is divided and constantly changing. The economic approach is unable to deal with changes in taste, or with the fact that people eat things they know they will later regret having eaten, and often wish there were a way of changing their short-term preferences.

When nutrition experts try to evaluate the overall adequacy of a nation's diet, they typically calculate caloric and protein intake per capita. These measures are quite useful in poor countries where a large portion of the population does not get enough to eat. They are less useful in rich countries, where most people get enough to eat and a great many people eat more than they should. In such countries progress may involve reducing caloric and protein intake, not increasing it. Nonetheless, trends in caloric and protein intake are of some interest even in rich countries.

In order to measure trends in food consumption meaningfully, we must take account of the changing age distribution of the population. Caloric intake per person fell from 1950 to 1960 in the United States, for example. This was not because adults ate less in 1960 but because there were more children in 1960, and children—at least small ones—eat less than adults. In an effort to minimize this particular problem I have assumed that children under 16 typically eat half as much as adults and have calculated food consumption per "adult equivalent" instead of per person.

Table IV shows that both caloric and protein intake per adult equivalent fell during the 1970s. The apparent decline in caloric intake is so small that it could easily be due to inadequate age standardization or other errors. The fall in protein intake is larger and is probably genuine. It is tempting to attribute this decline to hard times, but the actual reasons are more complicated.

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Table IV. Changes in Daily Food Consumption Per Adult Equivalent[a]

	1950	*1960*	*1970*	*1980*
Calories	3,788	3,811	3,934	3,895
Grams of Protein	110	115	120	115
Ounces of Meat (carcass weight)	—	9.1	10.0	9.0
Ounces of Poultry (ready to cook)	—	2.3	2.5	3.0
Ounces of Fish (edible weight)	—	.5	.6	.6
Ounces of Vegetables (except potatoes)	—	8.2	8.3	8.4
Ounces of Potatoes	—	5.7	6.1	5.9
Ounces of Milk	—	15.9	14.4	12.5
Eggs (number of)	—	1.1	1.0	0.9
Ounces of Refined Sugar	—	5.1	5.3	4.2
Value of Weekly Food Consumption in 1980 Dollars	$27	$30	$34	$33

[a] *Source:* Derived from *SAUS 1983-1984*, *Historical Statistics of the United States*, and *ERP 1984*.

Most Americans have eaten too much for decades. This does not mean no one goes hungry in America, but it does mean that overeating is more common than undereating. Americans became increasingly concerned about this problem during the 1970s. Exercise became fashionable, and diet books were constant best sellers. Doctors urged their patients to lose weight, and especially to reduce their intake of cholesterol. Under these circumstances we cannot automatically assume that people cut their food consumption just to save money. They may have been more interested in saving their lives.

One way to assess the relative impact of money and medical advice on food consumption is to look at what people stopped eating. Table IV shows, for example, that consumption of meat, milk, and eggs fell. Since all these items are high on cholesterol, it is tempting to assume that that was why people ate less of them. But meat, milk, and eggs are also expensive, so the test is hardly conclusive. Fish is a better test. If cost were crucial, fish consumption should also have declined, since fish prices are now even higher than meat prices. If health were critical, fish consumption should have risen relative to meat, since fish contains less cholesterol than meat. In fact, fish consumption remained constant, while meat consumption fell, suggesting that health considerations outweighed monetary ones. If cost cutting had been uppermost in people's minds, we would also expect to see a shift from green and yellow vegetables to potatoes. In fact, the trend was the other way. Consumption of refined sugar also fell sharply during the 1970s. All these changes suggest that health considerations had more impact on what Americans ate than economic considerations did.

Another way to decide why food consumption fell is to ask *who* cut back. If economic factors were critical, we would expect to find

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cutbacks among the poor. If health and appearance were critical, we would expect cutbacks primarily among the middle classes. We do not have reliable national data on who ate what prior to 1970. But the National Health and Nutrition Examination Survey (NHNES) gathered such data between 1971 and 1974 and again between 1976 and 1980. Comparing the two surveys we find that those above the poverty line slightly reduced their consumption of both calories and protein during the 1970s. Those below the poverty line, in contrast, hardly changed their protein consumption and increased their caloric intake. The same pattern recurs when we compare whites to blacks. It seems unlikely that the middle classes would reduce their food consumption because of budgetary stringency. Other expenditures, such as those on bigger houses, would surely be cut first. It seems more likely that middle-class food consumption declined because of concern about health and appearance.

None of this means that everyone was getting enough to eat during the 1970s. In 1974 the Gallup survey asked Americans if there had been a time in the past year when they could not afford to buy food. One respondent in seven said yes. When Gallup repeated the question in early 1984, one respondent in five said yes. This suggests that "hunger" increased between 1974 and 1984. But judging by the NHNES data, the increase probably occurred after 1980. This is what we would expect on other grounds. Unemployment rose sharply after 1980, and government benefits for those without earnings were reduced in many cases.

If we take an economic rather than a nutritional view of food, official statistics again suggest that consumption fell slightly during the 1970s. Table IV uses the Bureau of Labor Statistics' (BLS) food price index to estimate what it would have cost in 1980 to buy the market basket that shoppers bought in earlier years. Food expenditure per adult equivalent averaged $33 a week in 1980. (This includes eating out.) If shoppers had tried to buy the same mix of food in 1980 that they bought in 1970, Table IV indicated that they would have had to spend $34 a week. But shoppers *didn't* buy the same mix of groceries in 1980 as in 1970, for two reasons. First, the relative prices of certain foods had changed, which led shoppers to shift their pattern of purchases in order to get better value per dollar. As a result, shoppers could buy a market basket they regarded as comparable to their 1970 market basket for somewhat less than $34. More important, tastes had changed in ways I have already discussed.

How are we to assess these developments? If we take the conventional economic viewpoint, there was little change in the level of

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food consumption between 1970 and 1980. If the food price index compiled by the Commerce Department's Bureau of Economic Analysis (BEA) were a measure of "true" inflation, we could say that the level of consumption dropped 3 percent between 1970 and 1980. But because of shifts in relative prices, the BEA index slightly exaggerated the "true" rate of inflation. This may well mean that the level of food consumption was either stable or rose slightly.

From a nutritional point of view, however, the important changes between 1970 and 1980 were those that economists attribute to "taste." From a nutritional perspective the fact that people bought less meat, sugar, milk, and eggs in 1980 reflected not just the vagaries of "taste" but the fact that people had more information about the effects of eating these foods. Putting the point slightly differently, we can say that while the changes in food consumption between 1970 and 1980 would have looked like a change for the worse from the point of view of shoppers in 1970, who were relatively uninformed about the perils of self-indulgence, they probably looked like a considerable improvement from the point of view of shoppers in 1980, who were somewhat better informed.

The evidence I have reviewed on health, housing, transportation, and food hardly suggests that the 1970s were an economic catastrophe. Health improved more during the 1970s than during either the 1950s or 1960s. Housing improved at about the same rate as during the 1950s and 1960s. Transportation improved less rapidly than during the 1950s or 1960s, but it did improve. Food consumption fell slightly during the 1970s, but this appears to have been due primarily to increased concern with appearance and health. Ideally, it would be helpful to assemble analogous information about other areas of material well-being, such as clothing, home furnishings, recreation, vacations, and the like. In the absense of such data, however, the evidence regarding health, housing, and transportation suggests that we should scrutinize the Census Bureau's family income statistics more carefully. When we do this, three issues emerge as crucial: the proper correction for inflation, the proper way to define and measure income, and the proper correction for changes in family size. I will take these three issues up in turn.

Correcting for inflation

The Census Bureau has always used the Consumer Price Index (CPI) to correct its income statistics for inflation. By now almost every expert agrees that the CPI exaggerated inflation during the 1970s, because it treated the costs of home ownership in a very mis-

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leading way. In January, 1983, the housing component of the CPI was revised. Like its counterparts in other countries, the CPI now measures housing costs by measuring rents. This seems entirely reasonable. A "cost of living" index should measure the cost of living in a house, not the cost of investing in housing. Unfortunately, the published values of the CPI for years prior to 1983 have not been revised to incorporate this new approach. As a result, they still exaggerate the amount of inflation during the 1970s.

To get a somewhat more accurate picture of the rate of inflation, the Commerce Department's Bureau of Economic Analysis, which maintains the national income accounts, has for many years constructed its own deflator for converting what it calls Personal Consumption Expenditures (PCE) to constant dollars. The PCE deflator uses the same basic price data as the CPI, but it uses changes in rents to estimate changes in the price of housing, and it uses a slightly different set of weights to determine the relative importance of different items. Table V shows that when we measure income in "PCE dollars," median family income still rose 3 percent per year during the 1950s and 1960s, but it also rose 1 percent per year during the 1970s. Substituting the PCE deflator for the CPI thus reduces the apparent difference between the 1970s and the two previous decades by a third.

Table V. Average Annual Percentage Increase in Prices and Family Income[a]

	1950-60	*1960-70*	*1970-80*
Price Indices			
Consumer Price Index	2.1	2.8	7.8
Personal Consumption Expenditure Deflator	2.3	2.6	6.8
Median Family Income			
Current Dollars	5.4	5.7	7.8
Constant CPI Dollars	3.3	3.0	0.0
Constant PCE Dollars	3.0	3.2	1.0

[a] *Source:* Derived from *Money Income of Households, Families, and Persons in the United States (Money Income): 1980,* and *ERP-1984.*

But even the PCE deflator exaggerates the impact of inflation, because some of the goods and services available in 1980 were not available at *any* price in 1970. If we value these goods and services by asking what they would have been worth if they had been available, the answer is sometimes that they would have been worth staggering sums. In 1978, for example, my prematurely born son's life was saved by a drug that did not exist in 1970. In order to esti-

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mate the change in my "standard of living" due to this invention, one must calculate the amount of income that would have been needed to compensate me for the absence of the drug in 1970. Since *no* amount of income would have done this, my standard of living was "infinitely" higher in 1978 than it would have been in 1970 had my son been born then.

Conventional cost-of-living indices do not even try to take account of such technical innovations. As a result, we can seldom say anything meaningful about the rate of inflation in areas where technical innovation is important. The Bureau of Labor Statistics (BLS) calculates inflation in medical prices, for example, largely on the basis of changes in what physicians and hospitals charge for their services. BLS does not try to determine whether physicians' and hospitals' services improve as their charges rise. If, for example, it took the same number of physician visits and the same number of hospital days to treat Hodgkins' Disease in 1980 as in 1960, and if the cost of the course of treatment rose 200 percent, BLS would register 200 percent inflation. No correction would be made for the fact that most patients with Hodgkins' Disease died in 1960, whereas they were mostly cured in 1980. The national income accounts exhibit comparable myopia. To get a more reasonable approximation of people's intuitions about the value of medical services we would have to estimate "cost per cure" instead of "cost per treatment."

Similar problems arise in other areas. If people spent the same amount on home air conditioners in 1980 as on electric fans, cool drinks, and trips to air conditioned theaters in 1950, but were cooler in 1980 than in 1950, we ought logically to conclude that the price of staying cool had fallen. But our accounting system does not even try to measure the price of coolness, any more than it measures the price of health. The benefits of many technical innovations get lost as a result. This means we tend to overestimate inflation and underestimate the rate of improvement in the standard of living. Whether this bias was more serious in the 1970s than in earlier decades is unclear. I have argued that it was more severe for health in the 1970s and more severe for household conveniences in the 1950s and 1960s. I have no idea what a more thorough appraisal would show.

Correcting for reporting errors and taxes

The Census Bureau estimates family income by interviewing any "responsible" individual who is at home when the interviewer arrives. The interviewer asks this informant to estimate every household member's pretax money income from earnings, self-employment,

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dividends, interest, rent, and various kinds of transfer payments. Needless to say, this procedure leads to a certain amount of error. The Bureau periodically compares the total amount of income its respondents say they received from each source to the amount that relevant organizations say they paid out. This means comparing reported interest income to reported interest payments, reported wage income to reported wage payments, and so forth. These comparisons suggest that CPS respondents reported 84 percent of all money income in 1950, 87 percent in 1960, 88 percent in 1970, and 89 percent in 1980. If the Census Bureau were to correct its family income series for underreporting, the apparent rate of income growth would fall in all three decades, but the fall would only be noticeable for the 1950s (compare lines 1 and 2 of Table VI).

Table VI. Average Annual Increase in Aggregate Income Using Alternative Measures
(In Personal Consumption Expenditure Dollars)[a]

Income Measure	*1950-60*	*1960-70*	*1970-80*
Reported Income	4.0	4.6	3.3
Actual Pretax Income	3.6	4.5	3.2
Personal Taxes	7.2	6.4	4.3
After-Tax Income	3.0	4.1	2.9
Value of Government Services to Individuals	3.7	5.3	4.6
After-Tax Income Plus Services	3.1	4.3	3.3

[a] *Source:* Derived from *Money Income 1980*, *ERP 1984*, and Robert Eisner and David Nebhut, "An Extended Measure of Government Product: Preliminary Results for the United States 1946-76," *Review of Income and Wealth (1981).*

The Census Bureau's reliance on pretax income poses more serious problems. First, some income is counted twice. Pretax earnings, for example, include the employee's half of Social Security taxes. Transfer payments include Social Security benefits. Half of all Social Security benefits thus get counted both as employee income and as beneficiary income. Only the beneficiary gets to spend this income.

Pretax income is also likely to be misleading because governments spend a lot of their tax receipts on what economists call "intermediate" goods—goods that businesses use to make other goods—rather than on "final" goods for consumers. Highways (and many census statistics) are often used in this way. Including expenditures on "intermediate" goods when we calculate trends in the standard of living is a form of double counting. Defense spending should probably be thought of as an "intermediate" good too. Some might argue, of course, that fluctuations in military spending produce fluctuations in the public's feeling of "security." But the correlation

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between military spending and public perceptions of national security seems to be negative, not positive. This suggests that we spend more on the military when we feel threatened. Whether spending more makes us feel less threatened is unclear.

Table VI shows that personal taxes rose faster than money income throughout the postwar period. But taxes rose fastest during the 1950s, somewhat slower during the 1960s, and slower yet during the 1970s. This may surprise those who think of the 1950s as a period of fiscal conservatism. The image is correct in that legislators financed almost all government spending from taxes rather than borrowing during the 1950s. But it is incorrect if it implies that legislators refused to raise taxes during the 1950s. Defense spending rose from 5 to 9 percent of GNP between 1950 and 1960. In addition, suburbanization and the baby boom led to enormous increases in state and local spending on highways and education during this decade. As a result, pretax income, which is what people report to the Census Bureau, rose more than after-tax ("disposable") income during the 1950s.

While we must subtract personal taxes from income in order to avoid double counting, we must also add back something for the value of the free services that governments provide to individuals. When higher taxes provide better schools, cleaner air, better recreation facilities, or shorter driving time to visit friends and relatives, these improvements constitute income "in kind" to individuals. Estimating the value of these government services poses difficult conceptual and empirical problems. Table VI draws on Robert Eisner's estimates, which indicate that the value of government services to individuals, including both investment in their "human capital" (such as schooling) and expenditures on current services (such as parks), rose fastest during the 1960s, slower during the 1970s, and slowest of all during the 1950s.

When we adjust reported pretax income for underreporting, taxes, and the value of government services, as the bottom line of Table VI does, we see that total "true" income grew at exactly the same rate as the total reported to the Census Bureau during the 1970s, namely 3.3 percent a year. True income grew somewhat less than Census income during the 1960s, however, and a lot less in the 1950s. The effect of these adjustments is not, then, to make the 1970s look better than they do in the Census Bureau's family income series, but to make earlier decades look worse. Skeptical readers may be reassured to know that the "disposable income" series in the national income accounts, which also tries to measure after-tax

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income plus certain kinds of income "in-kind," tells almost exactly the same story as the last line of Table VI.

The income estimates in Table VI are national totals, not family averages, so they are not directly comparable to the figures in earlier tables. In order to make such income statistics tell us anything meaningful about the standard of living, some adjustment for the changing size of the population is obviously crucial.

Adjusting for population growth

The Census Bureau restricts the term "family" to groups of two or more related individuals living in the same household. This means that Census statistics on "family income" do not cover individuals who live alone or with non-relatives. The Census Bureau publishes a separate series covering such "unrelated individuals," but neither the Bureau nor anyone else pays much attention to this series. Since unrelated individuals constitute a growing fraction of the total population, and since their median income rose a lot faster than median family income in the 1970s, ignoring them can be quite misleading. The Census Bureau also reports family income without making any adjustment for family size. Since families averaged 3.6 people in 1950, 3.7 people in 1960, 3.6 people in 1970, and 3.3 people in 1980, failing to adjust for family size makes the 1970s look worse than they were. Unfortunately, there is no one ideal procedure for adjusting income statistics to take account of variations in family size. The correct adjustment depends on whether you want to measure the material standard of living or psychological well-being, and on whether you look at the problem from the perspective of adults or children.

Let us begin with adults' psychological well-being. If our aim is to measure adults' psychological well-being, the best thing to do about children is probably to ignore them. Most adults have children because they want them. If they don't want children they use contraceptives, get abortions, place their unwanted children for adoption, or—if they are men—leave home. Adults presumably spend money on children because they get more satisfaction from such expenditures than from alternative uses of the money. (Spaghetti eaten with people you love is usually more satisfying than steak eaten alone.) Because this is so, it makes no more sense to say that having children lowers an adult's subjective standard of living than to say that owning a yacht does. Children are expensive, and having children leaves less money for other things, but that is true of a yacht, too.

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Children do differ from other "consumer durables" in one crucial respect. If you buy a yacht and then find that you cannot afford the upkeep, or do not like it as much as you once did, you can sell it. Selling children who no longer give you pleasure is much harder. The likelihood that you will end up with more children than you really want is therefore higher than the likelihood that you will end up with more boats, cars, or houses than you want. As a result, the dollars you spend on your children may give you less pleasure than the dollars you spend on other things. The difference is small, however. Stephen Dubnoff and his collaborators have found, for example, that a family of three needs only 9 percent more income than a family of two in order to evaluate its income and its standard of living equally favorably. A family of four needs only 6 percent more than a family of three, and a family of five needs only 1 percent more than a family of four. This suggests that variation in the number of children parents have does not appreciably affect the way they feel about their income.

It follows that if our goal is to measure trends in adults' satisfaction with their income we can ignore the fact that people had more children in the 1950s than in the 1970s. From this perspective the best measure of economic welfare is income per adult. Table VII shows that this measure rose only 1.2 percent a year during the 1970s, compared to 2.0 percent a year during the 1950s and 2.7 percent a year during the 1960s. Using this approach, therefore, the 1970s look somewhat better than in the Census Bureau's family income series, but they still look worse than the 1950s and 1960s.

Table VII. Alternative Measures of Average Annual Percentage Increase in Aftertax Income plus Government Services[a]

Income	*1950-60*	*1960-70*	*1970-80*
Per Adult	2.0	2.7	1.2
Per BLS Adult Equivalent	1.5	3.0	1.9
Per Person	1.4	3.0	2.1

[a] *Source:* See Table VI, note a.

For many purposes, however, we care about trends in adults' *material* well-being, not trends in their *subjective* well-being. The line between the two is fuzzy, but there is surely a distinction. Spaghetti eaten with people you love may be more satisfying than steak eaten alone, but outside observers are still likely to say that a society in which everyone eats steak enjoys a higher level of material well-being than a society in which everyone eats spaghetti, no matter

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how miserable the steak-eaters are. If we want to measure adults' material well-being in this sense, we must subtract out the money adults spend on their children and consider only what they spend on themselves.

The Bureau of Labor Statistics publishes a "family equivalence scale" that purports to tell us how much money families of various sizes must have to enjoy the same standard of material comfort. According to BLS, a couple with two children needs 67 percent more income than a childless couple. This implies that adults spend about two thirds as much on their children as on themselves. BLS's rationale for this conclusion is merely that families with equivalent incomes on its scale spend the same fraction of their income on food. This rationale becomes more compelling, however, when we note that according to the Department of Agriculture's food budgets for individuals of various ages, if a couple with two children spends 67 percent more on food than a couple without children, the adults in the both families will end up eating equally well.[1] If the BLS scale ensures that adults in families of different sizes eat equally well, and if food has the same priority relative to other needs in families of different sizes, the families are likely to be equally well off in other respects as well.

If we assume that adults spend two thirds as much on children as on themselves, we can estimate trends in material well-being by counting children as two thirds of an adult and calculating trends in income per "adult equivalent." Table VII shows that this measure of material well-being rose 1.9 percent a year during the 1970s, compared to 3.0 percent a year during the 1960s and 1.5 percent during the 1950s. The increase in adults' material consumption was thus greater during the 1970s than during the 1950s, though still less than during the 1960s.

Income per "adult equivalent" is our best estimate of the material standard of living for children as well as adults. Whether it is also our best estimate of how children feel about the standard of living is harder to say. Those who favor large families might argue that while parents with lots of children cannot afford to buy their children as many material goods as parents with fewer children, children still benefit psychologically from having lots of brothers and sisters. I know of no empirical evidence that supports this view.

[1] The attentive reader may be puzzled by the fact that in my discussion of food consumption I assumed that children under 16 ate half as much as adults, whereas here I have asserted that it costs two thirds as much to feed a child as an adult. The difference derives from the fact that the BLS family equivalence scale includes children over 16 who live at home, and these children eat more.

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Among families of comparable socio-economic status, children from large families score lower on IQ tests, leave school younger, enter less prestigious occupations, and earn less money as adults than children from small families. This suggests to me that the decline in family size during the 1970s led not only to a rise in children's material well-being but also to an improvement in their subjective sense of well-being.

How are we to explain the fact that our measure of adults' material well-being (income per adult equivalent) rose so much faster during the 1970s than our measure of how adults evaluate their standard of living (income per adult)? One possibility is that when income per adult began to stagnate during the 1970s adults cut back the number of children they were having in order to ensure that their material standard of living would not stagnate too. This theory overlooks one crucial fact, however. The birth rate did not decline appreciably after 1973, when income per adult really began to stagnate. The big decline occurred during the late 1960s, which were a period of unparalleled affluence. The reasons for this change have never been satisfactorily explained, though theories abound.

What about the 1980s?

If the 1970s were not as bad as family income statistics make them seem, what about the 1980s? According to the Census Bureau, median family income, adjusted for inflation, fell 4.8 percent between 1980 and 1982. (No 1983 data were yet available as this was being written.) These statistics are clearly an unreliable guide to changes in material well-being. They do not take account of changes in personal taxes, government services, underreporting, or family size, and they make a misleading correction for inflation. Can we do better?

Fortunately, the Commerce Department's Bureau of Economic Analysis (BEA) publishes a more satisfactory measure of material well-being, namely "disposable income," which shows almost exactly the same trend from 1950 to 1980 as my measure of after-tax income plus government services to individuals. Furthermore, BEA estimates disposable income every month, and these estimates become available quite promptly. The Census Bureau, in contrast, publishes its estimates of family income annually, and the estimates for any given year are not available until late in the following year. According to BEA, disposable income per adult rose 1 percent between 1980 and 1982, while disposable income per adult equivalent rose 1.6 percent. The BEA and Census series thus tell quite different stories about the early 1980s, just as they do about the 1970s. Before

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accepting BEA's version of reality, however, we also need to look at direct measures of material well-being.

The direct measures of material well-being that were available for 1982 when I was writing this article mostly told a gloomier story than the disposable income series, though not so gloomy as the family income series. Life expectancy was the bright spot, rising even more rapidly between 1980 and 1982 than during the 1970s. Data on housing conditions in 1982 were not yet available as I was writing, but real interest rates were higher than inflation during this period, making home ownership less attractive, and this change may have slowed the increase in rooms per person. The recession also cut into home appliance sales, so improvements in this realm were probably slower than in the 1970s. Access to automobiles did not change between 1980 and 1982, but the median age of automobiles rose from 6.6 to 7.2 years. An increase of this magnitude over a two year interval must have led to some decline in cars' reliability. Food consumption also declined, following pretty much the same pattern as during the 1970s. People ate less meat, milk, eggs, butter, sugar, and potatoes, but more chicken and fresh vegetables. The only departure from the pattern of the 1970s was that fish consumption fell—and this decline was largely confined to canned fish. Weekly food expenditure per adult equivalent fell from $33 to $32 in 1980 dollars, however, and since relative prices did not change much, this almost certainly meant that shoppers were getting slightly less of what they wanted. The decline over this two year period is also too large to attribute to changes in taste. The Gallup data on people who could not afford to buy groceries, reported earlier, also suggest a substantial increase in the number of people who were not getting enough to eat.

In trying to reconcile the increase in disposable income with the decline in food consumption, appliance sales, and automobile sales, we need one piece of information that only the Census provides, namely how the *distribution* of income changed. Income increases among the rich hardly affect the measures of material comfort discussed in this article, because these families already have all the health care, housing, automobiles, and food they can use. Income increases among the poor, in contrast, have a substantial impact on many of the measures I have discussed.

From 1950 to 1980 the distribution of money income, as reported to the Census Bureau, was remarkably stable. The poorest fifth of all families had incomes about a quarter of the national average throughout this period, and the richest fifth had incomes about

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twice the national average. The distribution grew slightly more equal in the late 1960s and slightly less equal in the late 1970s, but the changes were extremely modest. This suggests that material well-being rose at about the same rate for the rich and the poor, though of course the absolute increase was greater for the rich.

From 1980 to 1982, however, income inequality increased substantially. After allowing for inflation (using the PCE deflator), the pretax money income of the richest 5 percent of all families rose 3 percent between 1980 and 1982. Meanwhile, the pretax incomes of the poorest 20 percent *fell* by 5 percent. The Census Bureau's measure of overall income inequality (the Gini coefficient) was higher in 1982 than at any time since the Bureau started computing it in 1947. Work by the Congressional Budget Office indicates that if we were to adjust these figures for changes in tax rates and government services, the trend toward greater inequality between 1980 and 1982 would be even more marked. It was almost certainly the deteriorating position of the less affluent that led to the sharp decline in food consumption and failure to replace aging automobiles. Preliminary reports indicated that inequality increased again between 1982 and 1983.

Statistics and personal experience

The reader may wonder why, if the material standard of living really rose significantly during the 1970s, so few people noticed. The answer, I think, is that inflation had a profoundly disruptive effect on the nation's psychic economy. Since nominal income was rising very rapidly, many consumers felt that they "ought" to be able to afford a lot more things. They had, after all, "earned" their pay increases. When their purchasing power rose only 1 or 2 percent a year they felt cheated, even though increases of this magnitude have been the historical norm. Since everything about the economy was changing at once, consumers also had great difficulty finding benchmarks against which to evaluate their progress. When some prices rise 50 percent and others rise 300 percent, it is bound to be hard to tell whether an income increase of 100 percent leaves you ahead of inflation or behind. When Ronald Reagan asked people whether they were better or worse off in 1980 than they had been in 1976, very few people could give an unequivocal answer based on personal experience, so they answered on the basis of what they saw on television and read in the newspapers.

Popular images of the American economy were almost uniformly negative during the 1970s. Inflation made people feel that the econ-

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omy was out of control—an impression that was surely correct. The narrowing of America's technological advantage also made American exports less competitive and encouraged imports, though overvaluation of the dollar probably played as large a role in these developments as technological change. In any event, the politics of boosterism, which had dominated America from the 1940s through the mid-1950s, were replaced by an apocalyptic politics in which all sides agreed that the country was in deep trouble and merely argued about whose fault it was. Good news no longer played much role in political rhetoric even when it was available. BEA's statistics on disposable income, which showed steady improvement during the 1970s, were largely ignored outside the business community. The Census Bureau's statistics on family income, which showed losses in many years, got far more attention.

None of this means that we ought to revive boosterism. The economy is still in serious trouble. Indeed, it seems to me in much worse trouble now than it was in the 1970s. But we have not been going to the poor house. Only the poor have suffered that fate. The rest of us should stop feeling sorry for ourselves and try to figure out what we can do to reduce the material hardships of those who really experience them.

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Why the "income distribution" is so misleading

MARK LILLA

AMONG social scientists, the yearly distribution of money income is one of the most frequently used measures of economic and social well-being. Whether expressed graphically (as a bell-shaped curve), in terms of averages (a certain percentage of the population receives less than half of median income), or in percentiles (people in the top X percent receive over Y percent of national income), this distribution is assumed to tell us a great deal about our social and economic reality.

But what is this reality? Frequently, the income distribution is taken to reflect something about the extent of "relative poverty." Even though, in the United States at least, we have rather complicated needs indices that are official poverty measures, many social scientists (and others) believe that one's relative position in the income distribution will make one feel and act poor, quite apart from objective needs. The income distribution is also taken to be our best indicator of the degree of economic inequality, which may be measured in a rough manner or with more sophisticated calculations such as the "Gini coefficient." Some go so far as to make this straightforward tautology: Economic inequality simply *is* an unequal distribution of income. Finally, underlying the concerns over both poverty and income inequality is the belief that income distribution is a

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matter of basic social justice, which may be measured, or at least approximated, with statistics. Even philosophy professors have come to address the original philosophical question—"What is justice?"—in terms of the social sciences, asking, "What is a just distribution of income?" and, "Is the distribution of income in the U.S.—or the West, or the world—becoming more or less just?"

Yet social scientists who make it their business to study the workings of the economy have understood for some time that the *idea* of "the income distribution" presupposed by these debates is somewhat problematic. To begin, all income that enhances economic well-being is not captured in the official income statistics. Net income, which would factor in government taxes and benefits (both money and in-kind), is undoubtedly a better measure, but is not always easy to calculate. Also missing is the implicit, "nonpecuniary" income produced within the family household; for example, a housewife's work in the home is not included, but if she works outside the home it is—even if she then must hire someone to fill her former "jobs" of housekeeper or babysitter. (In Third World countries much income is of this implicit kind, rendering official income statistics virtually worthless.) Studies that attempt to determine the value of this implicit income and then compute *real* net income are highly speculative, though they probably do give a "truer" measure of income.

A stickier problem is measuring life-cycle earnings. Since an individual's lifetime earnings typically follow an up-and-down pattern—low while a young adult, highest just before retirement, and then a leveling or reduction—there always will be a "natural level" of income inequality at any one time, if only because of the age distribution. Ideally, one would want to compute each individual's earnings in each year—discounted and adjusted for inflation—and then over an entire lifetime before comparing. Such a research project would be very expensive and difficult, so social scientists either have had to use special samples that make generalization difficult, or they have had to rely on the questionable econometric technique of "controlling" a cross-sectional income distribution for age and assuming that this corrected distribution represents the life-cycle distribution over a very long period. (In truth, no one knows.)

Researchers who specialize in the study of income and poverty fully understand these shortcomings of ordinary income distribution statistics, and usually compute "corrected" figures before studying these issues seriously. Ordinarily, however, these results can only be understood by the econometrically literate and bear an uncertain

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relation to ordinary conceptions of poverty, equality, and economic justice. The simple, official income distribution is easier to use than the "corrected" measures, so this is what nonspecialists—other social scientists, philosophy professors, public officials, political activists—generally do use. When social research enters the public realm, it is an axiom that, between a simple but misleading statistic and a complicated precise one, the simple one will always survive.

Income dynamics: the missing link

But even if we were able to produce a simple, problem-free, fully corrected measure of the distribution of American income, would it tell us what we think it should about the nature of poverty, equality, or justice? The simple answer is no, because the income *distribution* can never reflect anything about income *dynamics*. By dynamics I mean the processes by which individuals and families change their economic fortunes, processes that tell us something different from what their economic positions are at any one time.

To illustrate this distinction, imagine two economies with the same relative distributions of (net, fully corrected) income. Each year, economists studying the two economies take cross-sections of the populations and announce that the distributions are unchanged and identical. But in the first economy, let us say, everyone remains in the same position each year: If someone was in the ninetieth percentile last year, he will be there this year; if he was below the poverty level, there he will remain; and so on. In the second economy, however, everyone changes places each year. Indeed, every three years there is complete turnover in this economy, every family spending one year each in the upper, middle, or lower class; no one is rich for more than one year at a time, and no one is poor for more than one year at a time. Ordinary common sense tells us that our two hypothetical economies have very different poverty problems, have different levels or kinds of inequality, are not equally just. *But in terms of their annual income distributions they are indistinguishable.*

This seems very strange. But even a moment's reflection on such a simple example makes clear that the dynamics of income can be as or more important than its distribution—yet the former is an economic phenomenon about which social scientists know surprisingly little. There are, of course, countless studies of economic and social mobility, most relying on limited or specialized samples—for example, twins reared apart—to understand this fundamental economic process. Together they do not give a clear picture of this process, nor can they offer an economic theory of income dynamics. Real income

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dynamics among real families are difficult and expensive to measure, and the standard statistical methods for testing the data do not seem to apply. Consequently, the complicated questions of poverty, equality, and economic justice have remained on the Procrustean bed of income distribution.

Fortunately, a group of researchers at the University of Michigan's Survey Research Center has been working diligently for the past 15 years on the first truly adequate study of income dynamics in the United States (and perhaps in the world). Since 1968, under the direction of James N. Morgan and Greg J. Duncan, researchers associated with the Panel Study on Income Dynamics (PSID) have conducted lengthy yearly interviews with the heads of 5,000 American families—that is, the *same* families—in order to track the changes in their economic fortunes. The study is an extraordinary accomplishment, especially so given that these researchers have had to create from scratch many of the sampling and statistical techniques required to evaluate their unprecedented data properly. The study began with a sample of 5,000 families that was demographically indistinguishable from the American population as a whole. These families have been studied every year since 1968, as have the families that "split off," such as children living alone or starting their own families, widows and widowers, separated and divorced partners, and so on. (In fact, one of the most interesting results of the PSID is the insight it gives to the economic importance of these split-offs.) As of 1983 the panel included over 6,500 families, made up of roughly 16,000 people.[1] The survey itself gives us an exhaustive look at changes in each family member's important economic and social characteristics: income, wages, hours worked, births and deaths, marriage and divorce, education, unemployment, welfare use, and various attitudes toward economic mobility.

The PSID results have appeared in thick yearly reports, and occasionally in professional journals and newspaper articles as the panel has "matured." But now that 15 years have elapsed and the major economic patterns have emerged, the team has brought out a book summarizing its major findings.[2] In one sense, the empirical findings are nothing new. Common experience as well as previous

[1] Most lengthy panel studies become less representative over time, as panel members drop out. PSID has remained roughly representative of the U.S. population as a whole because the panel "reproduces" as new families split off, making up for lost cases in an unbiased manner.

[2] Greg J. Duncan et al., *Years of Poverty, Years of Plenty: The Changing Fortunes of American Workers and Families* (Ann Arbor: Institute for Social Research, University of Michigan, 1984).

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research on the "culture of poverty" and welfare use leave little doubt as to the importance of mobility in the American economy. The PSID methods and results are significant in a deeper, intellectual sense, though, because they make it clear that the idea of the income distribution tells much, much less than one would think about the economic condition of the American people. The "freeze-frame" character of yearly income distribution studies turns out to be more than a "simplifying assumption"; it is a real distortion that causes us to miss the truly dynamic character of open economies, and can muddle our thinking about poverty, equality, and economic justice.

Dynamic poverty

Take poverty, for example. Even though poverty is clearly more than a question of income, every official or academic definition of poverty in current use depends (explicitly or implicitly) on a fixed notion of the income distribution. Those families of a certain size that fall below a certain income level for a whole year are said, by definition, to be in poverty. Long-term and short-term poverty are to be distinguished as different social problems, but in any particular year they are said to be the same condition. There are ongoing debates inside and outside government over the level at which poverty is to be defined, and different federal and state agencies compute different family budget standards using the local costs of food, housing, clothing, and the like. Defining poverty in this way has notorious problems, among them accounting at the federal level for local price differences, valuing work in the home, including the value of different welfare benefits, and allowing for differences in "lifestyle."

Still, there are good, practical reasons for using such a fixed poverty standard. It allows government to decide easily how many people deserve benefits and how many people have been served each year; for program advocates, it provides a comprehensible —and, more important, a relatively stable—measure of the job still to be done. But can a fixed standard really tell us what we want to know about what poverty is and how public policy might cope with it? Most research on poverty has clearly shown that the long-term poor and short-term poor face dissimilar problems and opportunities, and that different sorts of programs and incentives may be required for these two subgroups. A simple income distribution cannot tell us the relative sizes of these groups. If a significant proportion of the people poor in 1984 were not poor in 1983, and will not

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be poor in 1985, then the character of American poverty is radically different from what it would be if there was no turnover in this population. This is not to say that the problem would necessarily be more or less severe; it is simply to recognize that the problem and the programs meant to cope with it would have to be conceived in quite different terms. Even simple political slogans such as "the safety net" and "social insurance" reflect certain assumptions about this underlying turnover rate in the poverty population.

A good deal of government-funded social research has focused on turnover in particular social programs, but until the PSID no single study has allowed a high level of generalization about turnover in the low-income population as a whole. For example, the PSID researchers were able to distinguish between those families that fall below the poverty threshold for a single year, those that are in the midst of a short, multi-year spell of poverty, and families that can be called the "persistently poor." These distinctions turn out to be highly significant (see Table I). Looking at these panel families over the ten year period 1969-1978, we see that the percentage of people in families that fell below the official poverty line in any particular year was relatively stable (in 1978 it was 6.8 percent).[3] But we also see that over those ten years nearly *one quarter* of those people fell below that level at least once. On the other hand, only 5.4 percent fell below the level during more than five of those years, and the persistently poor (eight or more years) were 2.6 percent of the population. Less than 1 percent of the sample came from families poor in all ten years.

These results are startling in several respects. Perhaps most surprising is that a large proportion of American families seems to fall below the poverty line at one time or another. This pattern has received the most attention from the PSID staff over the years, their most interesting finding being that this temporarily poor population is demographically indistinguishable from the population as a whole; it is a remarkably diverse cross-section of American families. And what leads to these spells of poverty is not some long-term social problem, such as lack of education, but rather short-term oc-

[3] Income includes government transfer payments. Although the PSID sample is representative of the whole U.S. population, its measured poverty rate has consistently been somewhat lower than Census Bureau calculations. Since investigations by independent researchers have not turned up a hidden bias in PSID methods, the Michigan team members suggest that their estimates may be *more* precise since they ask more thorough income-related questions, their interviewers and respondents have established a degree of rapport after many yearly sessions, and, since they are not from the government, they pose no threat to low-income respondents worried about losing government benefits.

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Table I. Short-Term vs. Long-Term Poverty, 1969-1978
(Percent of individuals in families with incomes below official poverty level)[a]

Poor in 1978	6.8%
Poor one or more years	24.4%
Poor five or more years	5.4%
"Persistently poor" (eight or more years)	2.6%
Poor all ten years	0.7%

[a] Percentage calculated from Panel Study on Income Dynamics sample. Adapted from Table 2.1, *Years of Poverty, Years of Plenty*, p. 41.

currences, most of them unplanned and many of them tragic. Among the most important discovered by the PSID researchers are marriage or divorce, illness or death of family head, birth of a child, and short-term unemployment. (One would probably have to include returning to school.) Generally, then, the short-term poor have suffered temporary set-backs leading to a drop in income, but can be expected to get back on their feet rather quickly.

The persistently poor represent a different population, and a different problem. But, surprisingly, they seem to represent a much smaller population and problem than has been thought hitherto. One of the most important findings of the PSID is that "*only a little over one-half of the individuals living in poverty in one year are found to be poor in the next, and considerably less than one-half of those who experience poverty remain persistently poor* [authors' emphasis]." To simplify somewhat, over half the poor represent a "turnover population" of the temporarily poor.

While the turnover population represents a rough cross-section of the American public, the persistently poor do not. The results are not surprising: The persistently poor are more likely to be elderly, black, rural, southern, and to come from families headed by women. But since the PSID follows the *same* families over the course of the study, it is possible for us to see which of these persistently poor families are most likely to improve their economic condition over time, and why. Among women, for example, getting married is the most promising route for leaving persistent poverty. More than half the income difference between black and white female-headed households was found to be explained by lower marriage rates among black women.

One must be careful not to draw one-sided conclusions from a study of this kind. If, for the moment, we accept yearly income as an adequate measure of poverty, then it is clear that poverty so defined touches a far larger number of families than is indicated by the

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standard statistics. However, for most of these families, "poverty" is not the beginning of social disintegration: Most keep their families together and return to jobs with sufficient pay. Persistent poverty, and the disastrous social consequences associated with it, is a much smaller (but perhaps more severe) problem than official estimates of the poverty population would lead us to believe.

The lessons for public policy that might be drawn from this study are many, and the PSID staff does a decent job of discussing a few of them. Since the study allows one to examine the dynamics of welfare families as they come on and off the rolls over a fairly long period, the suggestions regarding future welfare policy are perhaps the most promising. Their discussion of the relative insignificance of the "underclass" is least persuasive; that the long-term poor are a small fraction of welfare recipients, and that they seem indistinguishable from other poor people on the basis of a battery of psychological tests, cannot remove the reality of this destructive way of life, especially among minorities in our major cities.

But whatever policy recommendations are drawn from this study after the significance of its results is determined, the lessons regarding the income distribution are already clear. We now know what we have been missing by concentrating on ordinary annual income distribution statistics. The dynamics of poverty overwhelm its distribution. If all those falling below the poverty threshold in one year were to become permanently poor, we would face a grave social crisis, but the income distribution would remain unchanged. If economic growth and social programs succeeded in lifting almost all families out of persistent poverty, it would be a great achievement; but, again, the income distribution could remain unchanged. The income distribution is not just an imprecise measure of poverty, it is the *wrong* measure of poverty.

Dynamic equality

The case for using the income distribution as a measure of income inequality seems much better. Shouldn't the question of "Who gets what?" simply be answered by going around every year and finding out who indeed *got* what?

Now we hesitate. As with measures of poverty, measures of equality and inequality that fail to take income dynamics into account could be wildly misleading. Families may have been stuck in their same relative positions in that distribution over the past 40 years, or there could have been a great deal of upward and downward mobility. A "freeze-frame" measure of the income distribution cannot

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take such dynamics into account; whether that matters, though, will depend on whether those dynamics turn out to be significant.

In fact, the PSID sample indicates an astonishing degree of movement within the American income distribution. Taking the years 1971-1978, the PSID researchers find so much change that they sound frankly stunned. (Their results are summarized in Table II. The numbers represent the percentage of people in family income quintiles that remained in the same quintile, and the percentage that rose or fell to another.) They seem especially surprised to find so much mobility among the richest and poorest segments of their sample: "Of those who were either at the top or at the bottom levels in 1971, only about half had remained in those relative positions in 1978." In other words, *only about half of the best-off Americans in 1971 were still the best-off in 1978, and only about half of the poorest Americans were still poor*. Change in the middle income groups was even more dramatic: Only about a third of these families remained in the same place during the period, while the rest rose or fell. If there was little or no mobility within the American economic system, the numbers italicized in Table II would be close to 100 percent. As can be seen, none is higher than 56 percent. And all these changes took place in just seven years.

Table II. Changes in Family Income, 1971-1978
(Percentage of individuals in 1971 family income quintiles)[a]

Family Income Quintile, 1971	*Family Income Quintile, 1978*					
	Highest	*Second*	*Third*	*Fourth*	*Lowest*	*Total*
Highest	*48.5*	29.5	14.0	4.5	3.5	100%
Second	22.0	*31.5*	25.5	15.0	6.0	100%
Third	14.0	18.5	*30.5*	23.5	13.5	100%
Fourth	9.0	13.5	21.5	*34.5*	21.5	100%
Lowest	6.0	7.0	9.5	22.0	*55.5*	100%

[a] Percentage calculated from Panel Study on Income Dynamics sample. Adapted from Table 1.1, *Years of Poverty, Years of Plenty*, p. 13.

It is difficult to call all these changes real economic mobility, though; most people are not making or losing fortunes overnight (though clearly some must be). And most of this observed movement was from one income quintile to a "neighboring" one—from the third, say, to the fourth or second—so some of this movement may be short-term "noise." But the PSID does show that most significant income changes follow some major event such as divorce, death, marriage, birth, children leaving home, and so on. What seems to be true about the poverty population also seems to be true

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about the population as a whole: The income streams of most people are punctuated by years of high and low earnings, coupled with sudden changes in family size. These major events are especially significant for women, whose economic status is affected by both marriage and childbirth, making them the most volatile subgroup. For instance, one fifth of the sample's female heads of households unmarried in 1972 was married by 1978. These women saw their average family income increase $15,357 over that period, while the women who remained unmarried had an increase of only $864. Such changes among women point to a larger finding of the study, which is that, while the overall number and average size of American families change very slowly, particular families are changing constantly as members arrive and leave. These changes *within* each family, and their economic consequences, cannot be measured with ordinary income statistics that report on the "average" family, or the individual apart from his family.

So what the PSID results make clear is that, on top of the other measurement problems already mentioned, the income distribution has the additional handicap of not registering how, and at what rate, people change their relative economic positions. And those changes turn out to be terribly important: If the PSID data are indeed representative of the population as a whole, the "half-life" of the American income distribution (as measured in quintiles) is certainly no more than seven years, and is probably less.

Again, this is not to deny that many people stay rich or poor for an awfully long time. But now we know that there certainly is enough turnover in the system to make us think twice about what precisely we mean when we use income distribution statistics in speaking of income equality. To take a hypothetical example, if five families spend one year each in each income quintile, the income distribution might look terribly unequal over those five years; but wouldn't we have achieved a great deal of economic equality? Or, to take a less hypothetical example, we can compare two countries with relatively similar income distributions. If the first keeps most families in their economic place while the second allows much shifting of places, the second is surely more equal, even in strictly economic terms. But the international statistics all economists use —from the UN or OECD—cannot report this simple, crucial economic fact.

Dynamic justice

The more "precise" the income distribution becomes in statistical terms, the less interesting it becomes, the less striking it is in

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moral and political terms. And moral and political questions of economic justice are at the root of contemporary interest in the income distribution. Professors of moral and political philosophy who believe that equality of economic results—and not just equality of opportunity—is a question of political justice, find the income distribution a convenient, easily understood indicator of the justice of political regimes. They sometimes refer explicitly to this measure when discussing the limits of inequality in any fair distribution of money income, or they use the familiar bell-curve as a metaphor for the just distribution of all "social goods": income, property, wealth, education, health, status, and so on. The most familiar example of this is the work of John Rawls, who, in his *A Theory of Justice*, uses the fixed distibution as a metaphor to outline his "maximin" principle of justice, under which inequalities in a distribution are only justified if they make the worst-off the best off they can be.

The process of income dynamics examined above should give pause to those who unthinkingly use the idea of income distribution in these ways. Even if we were to accept the notion that economic status is a central question for political justice, it is unlikely that the current distribution of income would tell us much about justice so conceived. What is the proper accounting period for distributive justice? One day? One year? A lifetime? How are we expected to compare families of different size and composition? How are we to compare income over many years when people rise and fall so frequently? How are the "principles of justice," as Rawls calls them, to be determined in a distributive sense if people are constantly shifting places?

A defender of these distributive theories might retreat from such social generalizations and offer a hypothetical example. Suppose we have two people who work in the same office for their entire lives, who have families of the same size, and who encounter no significant accidents or tragedies—*ceteris paribus*, as they say. Yet one of these workers earns five times as much as the other. Leaving aside the important questions of skill, responsibility, productivity, experience—and, most recently, "comparable worth"—the distributive theorist wants to know: Is this distribution of income fair?

If one thinks dynamically about these matters, a plausible answer suggest itself: Fairness will depend, in some measure, on what happens to their children. If the sons and daughters, grandsons and granddaughters take up the same jobs as their ancestors, then this economic system will certainly seem unfair to those who define justice in this way. But what if their positions change in each generation? Should *that* matter in our thinking about distributive justice?

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We should recognize that this, at least, is *not* a hypothetical question. The PSID again proves its value by reflecting some of the intergenerational mobility in the American economy. The long-term nature of this panel study gives a clear window onto this phenomenon because, over the first 14 years of the study, nearly 1,500 young adults left their parents' families to begin their own. Thus it is possible to compare the economic status of an extremely large group of people with that of its parents.

Table III makes this comparison for those who formed new households by 1981. As one can see, *only just over a third of young adults with parents in the highest income group ended up in the same group, while less than half of those with parents in the lowest group remained there.* In the middle income groups there is no clear pattern, and the intergenerational distribution of income approaches equality. (Again, if the italicized numbers in Table III were all close to 100 percent, there would be no mobility, and hence no intergenerational equality.) If this pattern were to hold up throughout the lives of parents and children, that would mean that even a true distribution of lifetime earnings—if such a thing were available—would mask a tremendous amount of intergenerational mobility.

Table III. Intergenerational Economic Mobility
(Percent of young adults who formed own households by 1981)[a]

Parents' Average Family Income Quintile[b]	*Young Adult's Average Family Income Quintile*					
	Highest	*Second*	*Third*	*Fourth*	*Lowest*	*Total*
Highest	*36*	23	19	13	9	100%
Second	25	*26*	22	17	10	100%
Third	17	26	*23*	23	11	100%
Fourth	15	19	19	*24*	23	100%
Lowest	2	9	18	27	*44*	100%

[a] Percentage calculated from Panel Study on Income Dynamics sample. Adapted from Table 4.1 of Martha S. Hill, et al., "Final Report of the Project: 'Motivation and Economic Mobility of the Poor,' Part I: Intergenerational and Short-Run Dynamic Analysis" (Ann Arbor: Survey Research Center, August 3, 1983). Percentages rounded.

[b] Parents' and young adult's family income here is actually the ratio of income to an official needs index. This procedure corrects for family size and composition. Parental incomes are averaged over the years during which the children lived at home; children's incomes are averaged over the number of years during which they maintained independent households.

These results must be quickly qualified. The most severe limitation is that, although parents' and children's incomes are averaged over several years, neither income figure is expressed in terms of lifetime earnings; we have no way of knowing if the earnings of parents and children are more highly correlated at comparable stages of the life cycle—adult, parent, retiree. Furthermore, this PSID

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sub-sample may be slightly biased. For the parent-child pair to be included, the parents must be old enough to have young adult children, and thus are at the high end of their income stream, or are retired; the children, on the other hand, must be young enough to have living parents, which means they are in the early stages of their income streams. (How these biases balance out and affect the results is not immediately obvious.)

So the numbers in Table III must only be taken as suggestive of American intergenerational mobility—which is enough, since the point is only how misleading it is to think about income in steady-state, distributive terms. Finding the "real" rate of intergenerational change is less important than simply recognizing the dynamic aspects of income determination in the American economy, and that those intergenerational aspects cannot be ignored by the social scientist.

Does this go for moral and political philosophers as well? It is an interesting question, because it cuts across the distinction they ordinarily make between equality of economic opportunity and equality of result. If there is indeed economic opportunity, and if it has any concrete meaning, there should be less inequality of result when we look across generations. Yet contemporary moral and political philosophers, trapped by the idea of the fixed distribution, speak as if opportunity and result are mutually exclusive concepts, as if there is no *result* of opportunity over time. Underlying this distinction is the implicit assumption that the *individual* (in each year, or over his lifetime) is the only "unit" of moral analysis, and that the family has no special status in considerations of economic justice. Despite the many volumes recently written on the question of economic justice, to my knowledge no one has addressed intergenerational equity in this way.[4] One need not believe that any *inter*generational equality can justify *intra*generational inequities to see that those intergenerational dynamics must have something to do with what we mean by economic equality. If we return to our example of two countries with identical income distributions and discover that one has a high degree of economic mobility and the other has none, are we really willing to say that there is no moral difference between them?

We are not willing to say that because we know it is quite natural for people to think about the fate of their children and grandchildren when they consider questions of equality and economic justice.

[4] Interestingly enough, Rawls and others do discuss intergenerational *obligations*—with regard to savings, investment, preserving the environment—but not the difference between the justice of the intergenerational and intragenerational distributions of income.

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When parents save for education, or migrate to freer countries, or otherwise sacrifice for the economic well-being of their children, to no small degree it is because they see those children as extensions of themselves. One reason that Americans are so attached to the idea of equal opportunity—apart from strongly held notions of desert—is that they see it as a prerequisite for any *long-term* equality of result. For them, opportunity is not an abstract principle; it has concrete economic consequences. Shouldn't this "long run" outcome have *some* moral weight? While it is true, as a great economist wrote, that in the long run we are all dead, it should not surprise us that this same economist had no children to consider.

A post-distributive economics?

At stake in the study of income dynamics is more than another recalculation of the poverty level, or the reestimation of income inequality in the U.S. On both these counts the PSID staff has offered a set of highly suggestive results, but, like all such social science findings, they are open to modification and complication by other researchers. Such debate over these particular findings will be extremely valuable in future controversies over the shape of American social programs. But it would be a pity to stop there, because the significance of work on income dynamics for our thinking about economic matters generally, and about the research agenda of the economics community specifically, does not depend on these particular findings. (Indeed, the lack of imaginative discussion of these larger issues is the PSID volume's only real shortcoming.)

There has long been a critical tradition within the economics profession that insists that static economic concepts such as equilibrium and distribution are not raw facts, but rather *ideas* that simplify highly complex economic processes. The PSID research shows us just how limited ideas like this can be, and how misleading as well when applied to concrete social issues. The intellectual history of the distributive idea in economics, and its influence outside the profession, must be left for another time. For the moment it is enough to note how influential that idea currently is within the whole social science community, among other professors (notably philosophers), and even among public officials who unthinkingly depend on that idea in shaping social policy. Poverty, equality, and justice look quite different once the grip of that idea is loosened a little. Not that they look any simpler, or unproblematic; on the contrary, the dynamics of an open economy consistently upset our fixed notions of who the poor are, who gets what, and what is fair.

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These dynamics present a great challenge to the social scientist, whose research agenda and methodology have been profoundly shaped by the distributive idea. The intellectual investment in this agenda is great. Economists in particular operate under the assumption that the "movie" of an open economy is simply the sum of the "still shots"—that the analysis of long-term economic change is just a logical extension of the analysis of fixed economic states. Long-term industrial transformations are seen as the simple product of short-term maximizations by all firms; long-term changes in the American income distribution are the simple product of yearly income distributions. The non-dynamic assumptions underlying both these views are currently breaking down within the study of the firm, and the results look promising. Perhaps a similar reformulation of our debates over poverty, equality, and justice will be possible once social scientists realize that econometric and methodological gymnastics cannot make the income distribution the meaningful idea that they (and we) have thought it to be.

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American schools and the future of local control

DENIS P. DOYLE & CHESTER E. FINN, JR.

NO TERM in the lexicon of American education is more revered than "local control." Honored alike by the National Education Association and the Republican party, it is a phrase with iconic overtones, much like "academic freedom," "the three R's," and "equal opportunity." That local control is a good thing is assumed; that it may not be fully realized is acknowledged but regretted; that it distinguishes the United States from more centralized societies and more uniform political cultures is celebrated. Critics and dissenters are few and, perhaps, eccentric.

But does local control of American elementary and secondary education really exist? Is it an accurate description of the present and a satisfactory guide for the future? Or is it a cherished, but now anachronistic legend?

The sources of local control

Casual inspection of the ways public education in the United States is organized would seem to justify our speaking of local control. The primary unit is the "local school system," of which there were more than 15,000 in 1982. Each of these is overseen by a school board, school committee, or board of education, comprised of elected

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or appointed members, and virtually every one employs a "superintendent" or other salaried executive—sometimes popularly elected, more often appointed by the board—to administer the schools within its boundaries. The jurisdictions themselves range from minuscule districts with a single school and a handful of students—more than half the local systems enroll fewer than 1,000 pupils—to the vast pedagogical empires of New York City, Chicago, and Los Angeles.

Although they also vary in terms of true autonomy, all enjoy some formal independence from the general purpose governments of their communities. Some school districts have their own taxing authority, while others must go through the mayor or town council for their revenues. But all develop budgets, establish pedagogical priorities, identify areas of curricular and extracurricular emphasis, adopt regulations and procedures, and hire and fire staff members. Many also have authority over their school buildings—often including construction as well as maintenance—and most deal directly with state, federal, and private agencies. If something goes wrong, it is generally the superintendent of schools or members of the school board who will be the defendants in a law suit, not the governor or the city council. If a blizzard hits during the night, it is the local school system that decides whether to let the youngsters stay home in the morning, not the mayor or the state senate.

Yet, as with every other form of American "local" government, from sewer districts and transit authorities to the municipalities and counties themselves, local school systems are creatures of the state. The state constitution is the source and legal embodiment of the state's self-imposed obligation to provide education for its residents, and the legislature possesses plenary authority to discharge this obligation through whatever administrative mechanisms it likes—and to modify those mechanisms whenever it sees fit.

In part for administrative convenience, in part for fiscal reasons, and in part because of a history of community-sponsored public and quasi-public schools that, at least on the eastern seaboard, antedate the state constitutions themselves, 49 states have chosen to organize their public schools primarily into local systems, often coterminous with the general-purpose governments of cities, towns, and counties. Only Hawaii operates a single statewide public school system.

California, Illinois, and Texas each have more than 1,000 local school districts. Delaware and Nevada have fewer than 20 apiece. During the past half century, the number of local school systems has dramatically declined—from more than 100,000 before World

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War II to one seventh as many at present. The process of consolidation continues: 1,230 "operating districts" vanished into other districts between 1972 and 1982. But even though such amalgamations may be locally initiated—and essentially all of them must be locally acceptable—it is the state that wields the legal authority, and that must concur in such rare instances of increased localism as the partial decentralization of the New York City schools that took place in 1969.

The state also sets certain ground-rules for the public schools: the number of days they must be in session, the minimum qualifications that their teachers and administrators must possess, in most cases the core subjects that must be taught (particularly at the high school level), and sometimes the list of acceptable textbooks from which local districts must make their purchases. Though most state requirements historically have had relatively little to do with course content or academic standards, where they do apply they are voluminous and detailed, and a local school system that does not satisfy them may find itself in trouble. For example, students (or their parents) may be liable to prosecution under the state's compulsory attendance laws for not attending an approved school. It may not be legally permitted to confer high school diplomas. It could also be denied that portion of its budget provided by the state. For in addition to formal legal authority, most states wield enormous financial power over their public schools, such that the threat of losing state school aid money, like the prospect of a hanging, concentrates the minds of local school administrators and board members.

The rising state role: money

This was not always so. Prior to 1930, localities provided more than 80 percent of school revenues, the states less than 20 percent. Though the state share reached 30 percent just before World War II, it did not edge above 40 percent until 1973, by which time there was also a visible—though always small—federal contribution. The local share, which in 1973 was down to 50 cents of the school dollar, continued to erode during the past decade until in 1979, for the first time ever, the state share slightly exceeded the local contribution. By 1983, the local portion had dwindled to about 42 percent while the state share had risen to 50 percent (Washington supplying the remainder).

The state share still varies enormously from one jurisdiction to another, but the trend of the past ten years is unmistakable nearly everywhere. Excluding federal funds, in 1983 the state paid less

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than 40 percent of the public school bill in only nine states, while it paid two thirds or more in 14 jurisdictions. Moreover, the velocity of change was often dramatic. In just ten states did the state portion of school funding shrink between 1973 and 1983, and in only three of those—Pennsylvania, Maryland, and Minnesota—did it erode by more than 5 percent. In one jurisdiction (Rhode Island) the state-local balance held steady. In the remaining 39, however, the state share rose, and in 19 of these it grew by more than 10 percent. Particularly noteworthy were the increases in the state funding proportion in Montana (from 28 to 52 percent), Nevada (41 to 66), Washington (52 to 80), Indiana (34 to 63) and, above all, California, where the state portion of the state-local total was 37 percent in 1973 but 90 percent a decade later.

With due regard for the handful of jurisdictions that bucked the trend, the general conclusion is nonetheless clear: We must now begin to regard the states as the senior partners in the financing of public education, rather than as important supplements to predominantly local fiscal structures.

Several reasons may be adduced. Not being bound to the property tax, the states have many more sources of revenue, a significant capacity when school expenditures have soared even as enrollments have dwindled. Categorical state-funded education programs—for the handicapped, the gifted, the non-English speaking, the disadvantaged—have also been enacted by many legislatures. Interest groups—teacher unions, linguistic and ethnic minorities, crusaders for one or another kind of curricular emphasis or special program—have focused their efforts on state capitals and have often been rewarded by the enactment of laws favoring them, by promulgation of regulations benefiting them, and by the appropriation of state funds for programs serving them.

The rising state role: equity

The past two decades have also witnessed a separate but widespread effort to achieve greater social "equity" through purposeful reform of the financing of American public education, and (at least since the Supreme Court declined, in the *Rodriguez* case, to create a federal constitutional right in this domain) this effort has concentrated on the state capitals.

The school finance reform movement started with the proposition that the amount of money spent on a child's education should not depend on accidents of geography. Whether or not equal expenditures make for equally good schools or equivalent amounts of

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learning by the youngsters attending them (ample research makes plain that no such relationship can be assumed), simple justice would dictate that two children attending public schools in, say, Pennsylvania, should have roughly equal public resources devoted to their education, even if one resides in an impoverished coal mining town and the other on the Main Line.

So, at least, the theory goes. In practice, the reformers have had to contend with many ironies and inconsistencies. Sometimes a grimy industrial community has more taxable wealth—due to the presence of numerous factories, for instance—than the "lighthouse" schools found in exurbs 20 miles away. Still, the critics found plenty of large disparities. In California, where the school finance reform movement can fairly be said to have started, the Kern County school system of China Lake, located in a desert that was once the floor of a prehistoric sea, reported an assessed valuation of $100 per child in the 1960s—and even this sum was an artifact of a state constitutional provision requiring assessors to meet at least that minimum without regard to real value. At the other end of the scale was McKittrick School District, also in Kern County, whose agricultural wealth was exceeded only by its oil resources. For each of McKittrick's handful of children, there was a million dollars in assessed valuation. The outcome was clear: So long as school financing was primarily in the hands of localities, even a very high tax rate in China Lake would raise almost no money at all for education, while a minuscule rate in McKittrick yielded more money than school officials knew how to spend.

But if this disparity—and the less dramatic ones found throughout the state—gave rise both to a sense of inequity and to a theory of equalization designed to make amends, the long-term consequences of reform were not clearly predicted. The major triumph of the school finance reform movement was the celebrated *Serrano* decision, handed down by the California Supreme Court in 1967. The justices found the state's entire system of education financing to be unconstitutional because there was no compelling state interest in providing children in one school district with more money than those in another. The trial court was ordered to fashion a constitutionally acceptable remedy. It, in turn, directed the legislature to restructure the school financing system so as to bring expenditure levels for all California children within a band of $100. Given the actual disparities of property wealth and tax capacity, crafting such a solution was certain to require ingenuity and to encounter opposition—particularly in high wealth districts where "equalizing"

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meant capping or even reducing the amounts that could be spent on education.

The court did not tell the legislature precisely how to solve these problems or what approach to select, but it did sketch five "alternative methods" that it found worthy of consideration. Though these included "full state funding"—with the imposition of a statewide property tax to generate the huge revenues that would be necessary—the legislature and governor still had to function within the traditional political confines of "local control." Hence in the years immediately following *Serrano*, Sacramento officials faced a near-impossible task: Obliged on the one hand to play Robin Hood, redistributing the resources available for public education so that these would be nearly equal from one district to another throughout the state, they were effectively barred by custom and by politics from taking the bold measures necessary to carry out the court's mandate in a tidy and efficient manner.

Enter Proposition 13, a truly "non-incremental" change in the basic assumptions of California's public sector. So far as we can determine, no member of the school finance reform community endorsed the "Jarvis-Gann" initiative. Indeed, that classic expression of the populist-conservative "tax revolt" impulse was anathema to liberal reformers. Neither did the state's political power structure support it. Proposition 13 was an object of fear and loathing in the eyes of practically everyone committed to school finance equalization and, indeed, to nearly everyone actively engaged in public education.

Yet Proposition 13 has had the effect of transforming California from a state in which most school revenues were raised locally into one in which the lion's share of resources for public education is now channeled through Sacramento. Today, only Hawaii (with its statewide school system) has a larger "state share" than California. The need to keep the public schools functioning, notwithstanding the shackles that Proposition 13 placed on the local property tax, has had very nearly the effect the *Serrano* reformers dreamed of: the *de facto* creation of a unified and uniform statewide public school financing system. To be sure, much the same thing has happened to other public services that were once principally paid for and run by local government in California. And it is never safe to characterize California as "typical". But our most populous state sometimes offers a preview of the future. In this case it certainly demonstrates what is apt to happen when a move to equalize school spending collides with a move to reduce the burden of local property taxes.

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The "excellence" movement

Meanwhile, an altogether separate but very powerful wave of education reform has begun to wash over the states. Sometimes dubbed the "excellence" movement, it is a complicated effort to reverse decades of declining test scores, of sagging indicators of teacher competence, of softening pupil performance standards, of proliferating electives in the curriculum, and of mounting numbers of high school "graduates" entering college or the workforce without having mastered the habits, skills, and knowledge deemed necessary for success.

Unlike earlier waves of education reform, the federal government has had practically nothing to do with this one, save for creating the National Commission on Excellence in Education, whose stern criticisms and stirring rhetoric helped define and legitimize the excellence movement. Although several other of the proliferating national task forces and commissions that have recently appraised and reported on elementary and secondary education did urge Washington to assist with the training of science and math teachers and to mount various other programs, most of the actual reform activity is taking place at the state (and, to a lesser extent, local) level. Here, the future was previewed in the south, where a handful of governors—notably Virginia's Robb, North Carolina's Hunt, Florida's Graham, Tennessee's Alexander, Mississippi's Winter, and Arkansas's Clinton—deduced that the economic development of their impoverished states depended in significant part on better education and set about to devise sweeping changes in school policies and practices, together (in most cases) with additional taxes to pay for them. The southern governors have been joined—or mimicked—by others from New Jersey to Alaska, by state legislative leaders, by business "roundtables," by citizens' task forces, and by newspaper editors. In a few cases, prominent educators—the most visible and effective of these being California state superintendent of public instruction Bill Honig—have seized the reins, but most of the reform impetus has been supplied not by the education profession but by laymen and elected officials.

These state-level education reforms display two general characteristics. They envision much more statewide homogenization and regulation of public school norms, standards, and procedures. And they include substantially increased education spending by state governments. Many of the reform plans are comprehensive, multipart schemes, ranging from computer literacy to the retraining of school principals, from changes in high school graduation requirements to summer programs for gifted youngsters, from statewide

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basic skills proficiency tests for sixth graders to mandatory foreign language study for tenth graders. The policy packages differ, but practically all of them include new state-set and state-enforced performance standards for both students and teachers. And while some of these standards are tied to quantitative changes in school inputs and processes, most of them relate to qualitative criteria: can the student—or the teacher—achieve such-and-such a score on such-and-such an examination?

In the past, one has had to look long and hard for serious statewide standards of individual performance. Many states stipulated that high school students had to take three or four "units" of English and a year of American history before they could graduate, but the content of those courses was almost always left to local discretion, as was the appraisal of pupil performance. New York had its "Regents' Examinations," of course, but few states prescribed what or how much a student actually had to learn at any particular stage of his schooling. As for teachers, state "certification" is a long-established procedure, but it has been virtually meaningless. Any graduate of an approved program of teacher education—which generally meant of any teachers' college—was automatically eligible for a license, as was anyone else whose transcript matched a list of course requirements promulgated by the state department of education. New teachers did not have to pass a test of ability or knowledge, nor did they have to demonstrate their classroom prowess to anyone but the university that supervised their practice teaching. Once a teacher had a license, he could ordinarily expect to keep it for life.

At the present time, however, most states are moving rapidly to develop and enforce performance standards for teachers as well as pupils. A survey in the fall of 1983 revealed that 30 states had adopted (though not all had yet put into effect) testing programs for persons wanting to be licensed as teachers, and a dozen more were actively considering that strategy. The Arkansas legislature even voted to require *veteran* teachers to take such an examination—and threatened to take certificates away from those who failed. By early 1984, Florida, California, and Tennessee had all adopted statewide variants of the "master teacher" idea, whereby particularly effective teachers may gain added responsibility, pay, and (presumably) status. Several other states were weighing radical changes in the concept of teacher certification itself, typically moving to allow into the classroom individuals who had not graduated from colleges of education but who might nonetheless be good instructors.

In late 1983, a survey conducted by *Education Week* showed that in the previous two years, 26 states had stiffened their require-

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ments for high school graduation, that about half were considering lengthening the school day or school year or otherwise increasing the amount of "instructional time," that ten were contemplating limits on extracurricular activities, and that seven were considering joining the 19 states that had already begun to require students to pass an "exit test" before receiving their high school diplomas.

Regulating for excellence

All such reforms narrow the scope of local sovereignty and enlarge the domain of state regulation. Though they do not necessarily alter the formal organization of public education, they leave less to the discretion of local boards and superintendents. They use both carrots and sticks to move the education buggies at a faster average (and more uniform) speed: the carrots of state funding, the sticks of formal regulation and of public opinion aroused by charismatic governors, hounding newspaper editors, and the potential embarrassment resulting from publication of district-by-district and school-by-school scores on state-mandated tests. Furthermore, where the localized structure of public education has proved inefficient or inconvenient, state leaders have shown their willingness to disregard it, establishing statewide schools for gifted youngsters, regional summer programs, state "principals' academies," state-organized "audit teams" that sweep in to scrutinize the activities of sub-standard schools and school systems, and state-run teacher evaluation programs that actually send observers into individual classrooms to appraise teacher performance. Kentucky has recently adopted what might be termed the ultimate solution: an "academic receivership" plan under which the state can assume direct control over and management of any local school system that repeatedly fails to meet minimum educational standards.

Local school administrators are already feeling pressures from their state capitals—and noting the relationship between funding and regulation. "Every time there's a recognition of a problem, the Legislature mandates a course," observed Clair Burns, the Norton, Ohio school superintendent. "If the Legislature [also] determines levels of competency, it won't matter too much what the communities want." Adds Cuyahoga Falls superintendent Harold Wilson, "[T]he more money the state Legislature puts into primary and secondary education, the more they're going to have a say in how it's spent. So unfortunately, the more we look to the state for money, we may be giving up the right to make decisions."

If the reform pace is maintained at the state level—and in mid-1984 there is ample reason to suspect that it will be—the results may

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or may not include more children acquiring more knowledge, but they will definitely include a marked increase in state regulation, direct state administration, and elaborate statewide monitoring and accountability systems, together with a continuing rise in state education spending. As these structures are created and funds are appropriated, the governors and legislators will become less likely —indeed, less able—to lose interest, to relax their grip, or to allow a resurgence of localism. Public elementary and secondary education already consumes approximately 35 percent of the average state budget, and the education department is frequently the largest and costliest branch of state government. As it gets still larger and more expensive, we are ever less likely to see a revival either of significant local sovereignty or of the ostensibly non-political "lay board -professional staff" governance structure that has characterized most statewide education policy-making. It is already common for governors to have education policy advisors, on their staffs and in their cabinets, who are at least as influential as any "chief state school officer"—the senior professional who heads the state education department under the aegis of a board of regents or state board of education. One also finds more education policy specialists on the staffs of state legislatures, state budget offices, and the like.

Such specialists were visible years ago in states (such as New York) that have long engaged in minute statewide regulation of schools, and the combination of *Serrano* and Proposition 13 has caused an increase in the number of such "experts" in Sacramento. But they are now needed as well in places like Tennessee, where in early 1984 the legislature found itself grappling with a "comprehensive education reform" bill of some 80 pages, not including 40 additional pages of amendments. It was not just the length that made the bill unwieldy; so intricate were the provisions, and so many "moving parts" did the legislation contain, that the real challenge came in trying to understand what effects an amendment to one section might have on the operation of a seemingly unrelated provision. The legislature had not previously had to deal with anything so complex, and it faced a crisis of institutional competence as much as of political resolve.

The "excellence" movement continues apace in the state capitals, and the school finance reform movement, which had never ceased filing lawsuits and urging legislative changes in aid formulas, is now struggling to make common cause with the quality-seekers. This is not a hopeless undertaking, for the advent of strict statewide performance standards for youngsters and school systems

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strengthens the argument that the state must therefore "equalize" the opportunities for all students to attain those standards. One obvious way to do this, albeit not the only one nor necessarily the best, is to equalize expenditure levels—and then, perhaps, introduce purposeful inequalities to pay for extra services to those whose performance is farthest below the standards. Moreover, the additional revenues to be raised by the states via the tax packages that usually accompany reform legislation provide a rare opportunity to achieve more equal spending levels without "leveling down" the most prosperous communities.

What about diversity?

It is therefore reasonably clear that the traditional pillars of local control—funding, setting standards, and determining educational content—are tottering. Somewhat less clear is whether this is educationally desirable. There are at least three reasons to suspect that it may not be.

First, state education departments are notoriously sluggish and formalistic bureaucracies, hardly the kinds of public agencies one would happily entrust with responsibility for sustaining a reform movement or for administering anything so unpredictable as a school or so loosely-coupled as a school system. It is hard even for the principal on the scene to alter what actually transpires in the teacher's classroom, and demonstrably difficult for superintendents and local school boards to affect what happens in the principal's office. At least in large school systems, the worst schools seem impervious to direction from outside, while the best are usually led by canny "outlaws" who figure out how to get things done outside the regulations and procedures set forth by the "central office." It is not likely that such a system will respond well to detailed regulation from the even more remote reaches of the state capital.

Second, much recent research into the characteristics of unusually "effective" schools makes plain that such institutions nearly always manifest a highly developed school-level ethos—some scholars term it a "shared moral order"—that has been cultivated over the years by administrators, teachers and often parents and students working together as a team to devise common goals and satisfactory procedures for achieving them. These characteristics are embedded deeply in the organizational culture of the individual school, they are largely "home-grown," they are virtually impossible to mandate from on high, and they are fragile enough that they could easily be damaged by attempts to achieve greater uniformity throughout the

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system. This is already a problem within large local school systems; it is apt to be aggravated by firmer statewide regulation.

Third, the foremost virtue of "local control" is that individual school systems have been able to distinguish themselves in modest—and occasionally large—ways from other school systems, and the existence of these differences has allowed some responsiveness both to community priorities and to the yearning of individual families to select the kind of education that their children will receive. Although public schools throughout the United States are much more alike than they are different, it has been possible for some families to settle in Newton rather than Quincy, in Evanston rather than Skokie, even in Queens rather than Brooklyn, at least in part because they perceived a sufficient difference among the schools to warrant such a choice. Sometimes the differences are elemental: pupil safety rather than schoolyard violence. Sometimes they are ignoble: avoidance of racial integration in one community by moving to another. Sometimes they are nearly frivolous: an athletic child has a better chance of making the team in one high school than in another. And sometimes they may even seem a bit esoteric: a better "special education" program for learning-disabled children, the presence of a particularly solid math-science curriculum, or the availability of a preprofessional school for musically gifted youngsters.

Whatever the reasons, and however laudable the basis for making the choice, such perceptions of diversity among schools and school systems have surely kept within public education some families who would otherwise have fled, have certainly influenced a host of non-education decisions (such as where to locate corporate headquarters and plants), have embellished the career reputations of a number of educators, have both simplified and complicated the tasks of college admissions committees, and have enabled the public educational system to respond in part to the variegated educational and cultural values of different communities, which in turn retain some of their distinctiveness—and thus perhaps some of their cohesion—because it is mirrored within the schools their children attend. At a time when a number of local systems are moving to establish "magnet" schools and other means of enhancing diversity, and when advocates of vouchers and tuition tax credits assert that still bolder structural changes are needed in order to provide true choices to more parents and children, any move toward greater educational homogeneity and statewide uniformity is bound to produce disquiet among those who favor the opposite.

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Why local control fails

Do such concerns create compelling arguments to combat the tendencies of the state to supplant localities in both financing the public schools and setting policies and standards for them? Probably not. In the event, resistance might well prove futile. As noted above, the state has the formal constitutional responsibility for public education and thus has long had the power to decide what to delegate to local systems and what to retain in the capital. Moreover, there are sound reasons for state governments to ensure at least minimum levels of funding to all schools within their borders. Though limiting the maximum sums that a wealthy community may spend on its schools is naturally controversial, state provision of minimum resource levels is obviously reasonable. There is little relationship between the value of property in a given community and the educational needs of the children who live there. Some rough justice can be found in the old public finance maxim that property taxes should support property-related services, such as police and fire protection, roads, water, and sewers, not services that by their very nature embody investment in the human capital of the entire society. And, as myriad additional responsibilities have been thrust upon the public schools by the concerns of a society that is more complex than any one community—as they have become multi-purpose social service agencies and as their curriculum has been stretched to accommodate dozens of specialized interests—it is even less realistic to suppose that all the associated costs should be borne by the immediate community. The obvious alternative, perhaps the only real alternative, is to support the public schools primarily through revenues generated by broad-based statewide taxes.

As for education policymaking, although "local control" produced a handful of superb individual school systems scattered across the country, and a larger number of fairly decent ones, the average "quality" of American public education has been too low and sinking for too long, and the nation's thousands of local school board members and superintendents did not, in the main, respond satisfactorily. Even today, amid the "excellence" movement and in the aftermath of all those commission reports, polls of local school board members reveal them to be far more concerned about what they deem to be inadequate financing and insufficient parental support for schools than about pedagogy or the quality of the curriculum. In other words, school board members are more apt to lament circumstances over which they have little or no control than to apply themselves within the many policy domains where they have im-

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mense leverage. Too many school board meetings are devoted to the approval of bus routes, purchasing orders, and maintenance plans, and to the resolution of disputes, while too few are given over to the content of the school program, the standards of student performance, the adequacy of the teaching force, and the provision of effective instructional leadership by principals and supervisors. Local school boards, in short, have with rare (albeit welcome) exceptions *not* moved vigorously to diagnose the qualitative maladies of their schools or to prescribe remedies. And it is that neglect, compounded by the failure of the education profession to frame the right questions and suggest the best answers to the laymen on the school boards, that has prompted state officials to seize control of the process of educational reform.

Alternatives to local control

If, then, this shift of the center of school governance from the locality to the legislature is all but inevitable, if it is in certain respects desirable, but if it simultaneously menaces (or is oblivious to) some of the singular virtues of school-level sovereignty and educational localism, is any resolution possible? Can we gain the benefits of enhanced statewide financing and policy-setting without acquiring all the disadvantages?

The first sign of wisdom is to acknowledge that "local control of public education" as traditionally conceived is in reality disappearing, even though its facade is nearly everywhere intact. What appears to be happening is that local school systems are evolving in practice into something that they always were in a constitutional sense: subordinate administrative units of a state educational system, with some residual power to modify statewide regulations and procedures in order to ease their implementation within a particular community, and with the residual authority (in most states, though not all) to supplement state spending with locally raised revenues.

If we acknowledge that except in a few small states it would not be feasible for a single central bureaucracy successfully to direct the day-to-day affairs of thousands of schools, tens of thousands of school employees and hundreds of thousands of children, and if some sort of administrative decentralization is therefore necessary, we can still fairly ask whether the current form of organization makes sense.

In terms of organizational efficiency, the present pattern of local school systems and boards has some obvious failings. The grossly uneven size of local units means that some have vast, unwieldy bu-

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reaucracies of their own while others are too tiny to realize the economic and educational benefits of a larger unit. Divergent economic conditions, even in neighboring communities, yield the fiscal inequities already noted in connection with the movement to reform public school finance. The pupil attendance barriers between adjoining districts bedevil plans to foster social integration and may also interfere with family educational choices, save for those so wealthy and mobile as to be able to relocate the entire family from one town to another. And, of course, the political psychology of local control insulates the least successful school systems from statewide educational improvement efforts, even as it buffers the best schools from state-imposed folly. Perhaps the most vexing feature of the current system, however, is its inattentiveness to the importance of *school-level* educational decision-making, its inability to devolve vital decisions about pedagogy, standards, and curriculum to the "school team," and its insistence on uniformity across all the schools located within a community. This existing problem can only be compounded when statewide norms and uniform procedures are superimposed on those devised locally.

Assuming that some continued decentralization is nonetheless needed, that the "Hawaiian" statewide model is impractical in large states, but that the status quo is unsatisfactory for the reasons suggested above, we find three alternatives that invite consideration.

The least attractive of these may be termed "modified centralization." The state education agency would run all the public schools, but would do so predominantly through bureaucratic sub-units designed to correspond to geographic divisions of the state. These may be few or numerous, and the subdivisions may have local advisory councils to make recommendations with respect to various matters in which the regional offices would have some discretion. But responsibility and authority for the schools would be borne by the state (that is, by the governor and legislature), and the "chain of command" would not have any breaks in it from the school house to the statehouse. This is not so very different from the way a multicampus state university is organized under a single board of regents, nor is it much different from other large state social service agencies.

A bolder and more engaging strategy might be called "rationalized regionalism." The public schools would be regrouped into larger units than at present, each unit to embrace an entire metropolitan area or sizable swath of countryside, such that even a large state would have fewer than 15 of them and most would have half a dozen. Each unit would have its own elected board and appointed

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superintendent, and each would receive from the state the equivalent of a "block grant" of money together with a set of educational "performance standards" that it must achieve. So long as it meets those standards within the funds available to it, the unit can organize and conduct its affairs with nearly complete autonomy. It can take Mortimer Adler's *The Paideia Proposal* as a model and run identical schools, or it can turn every building into a "magnet" school altogether different from other schools in the unit. It can put its teachers onto a "career ladder" or it can employ a traditional salary scale. But all students will regularly be tested by a board of "external examiners" engaged by the state for this purpose, to see whether their performance meets or surpasses minimum state requirements. If it does, the unit retains its autonomy. If it does not, then (as in Kentucky) the state education agency may assume direct control, at least until the situation can be rectified.

Under both of these approaches, funding levels and minimum performance standards would be uniform throughout the state. Educational units would be large enough to realize economies of scale. But the difference between the two strategies is significant: Modified centralization assumes a single statewide school system, while rationalized regionalism, having redrawn the boundaries of the "locality" to reflect late twentieth century metropolitan patterns rather than mid-nineteenth century towns and villages, then confers on those regional systems far greater autonomy from the state than most local school systems enjoy today. Rather than administering or regulating the day-to-day affairs of the schools, the state would supply funds, set minimum outcome standards, and monitor the performance of the regional school systems in relation to those standards.

A radical alternative

There is, however, a third alternative, bolder than either of these and to us more compelling. It is to construct a statewide public education voucher system and to finance it completely with state revenues. Under such a plan, all public education funds would attach to individual students, not to institutions, and families would select the schools that best suit their children's educational needs. Individual schools, in turn, would virtually run themselves.

This strategy rests on a controversial assumption, namely that higher quality education is more apt to result from a system in which all parents are freely able to make such selections from an array of schools that are actively seeking to attract students, than

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from a centralized bureaucracy that prides itself on uniformity and impersonality. So long as the state sets minimum standards to which all participating schools must conform and insists on "full disclosure" of information according to categories and criteria by which schools can be compared, we are reasonably confident that competition need not produce charlatans, deceptive advertising, or chronic institutional instability. We do not hope to persuade those whose foremost educational values are organizational stability and uniformity or whose own careers depend on the bureaucratic machinations of large local school systems. The public, however, *is* persuaded, as many recent opinion polls (most conspicuously the 1983 Gallup education survey) make clear. Renewed popular interest in vouchers led the Minnesota legislature in 1983-1984 to consider a limited program (for low income families) and there will likely be a referendum to create a statewide voucher system on the Colorado ballot this November.

We will not attempt here to settle the many details that must be carefully resolved before any full-fledged voucher program could be put into place. These include such fundamental matters as the nature and extent of state "standards" for participating schools, the procedures for handling admission to those schools that have more applicants than they can accommodate, the implications for teacher qualifications, contracts, and tenure, the precise governance structures of individual schools, the possible "weighting" of voucher values to take account of children with special educational needs and the differing costs of various curricula, and the peculiar problems of youngsters in rural areas that are too thinly populated to support competing schools. Nor will we examine the variations on this scheme that might include some of what are today regarded as "private" schools. (Under certain types of voucher plans, the traditional distinctions between public and nonsectarian private schools would practically vanish.)

A statewide public school voucher system is not without complexity and risk. But it clearly has the potential to meet several important objectives, including the consummation of school finance reform, such that similarly-situated children would have identical resources devoted to their education, wherever they may live within the state. (This was actually anticipated by the California Supreme Court in its widely-forgotten suggestion that "vouchers" were one plausible form of compliance with the *Serrano* mandate.) Such an approach could also facilitate the establishment and enforcement of statewide quality standards, and their appropriate application

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through well-publicized measures of school performance, rather than through bureaucratic control. A further virtue is the provision of true educational choice for all youngsters, regardless of their families' financial circumstances, race, or heritage. In fact, a statewide voucher plan would entirely eliminate the most vexing barriers to racial and socioeconomic integration of the public schools, namely the geographic boundaries of today's local school systems. Finally, vouchers would reinvigorate the principle of "local control" at the level where research and common sense show it to have the greatest educational significance: the individual school, with its unique population of teachers, administrators, children, and parents.

From district to school-level control

We propose, then, to give new life to a doctrine of educational governance in the United States that is sickly and weak if not yet moribund. Local control of public education as conventionally defined is an antiquated doctrine. It is the organizational legacy of a stable, agrarian society in which the financing of schools was an obligation of the immediate community in which those schools were located, and in which the establishment of educational policies and the enforcement of educational standards were likewise the duties of the village, town, or county, subject only to the statewide constitutional provision that no locality could ignore those obligations.

Today, the primary source of fiscal and political energy in the public education system is to be found in the state capital. This in itself is an unaccustomed situation for students and practitioners of education policy, who for two decades have tended to focus on developments in Washington and to suppose that any large changes would take place at the behest of and with funds provided by the federal government. This is manifestly not the case at present, with respect either to the financing of public education or to the "excellence" movement that is striving to elevate school standards and educational quality.

Yet the governance structure has not changed to reflect the new financial and political circumstances, and if it does not change we are certain to witness unrelenting guerrilla warfare as state and local officials each seek to minimize the power of the other while maximizing their own control, each certain that it has on its side both the best interests of the children and the time-honored principles of educational governance. The localities will lose most of these battles in most jurisdictions because the states have greater resources, stronger legislative levers, and ultimate constitutional authority.

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But the battles will themselves consume much time and political energy that might better be devoted to the improvement of teaching and learning.

Local control of public education, as traditionally conceived, has a dim future, if only because it is ill-suited either to a mobile modern society or to the contemporary realities of educational finance and politics. But school-level control of the essential elements of teaching and learning holds enormous potential for the improvement of American education.

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The untold story of Reagan's "New Federalism"

RICHARD P. NATHAN & FRED C. DOOLITTLE

IN THE 1984 presidential campaign, there has been a great deal of discussion of economic and foreign policy, but very little mention of domestic social policy. While the Reagan administration placed considerable emphasis on social program changes at the outset of its term, it has not continued to do so. And the Democrats, meanwhile, are downplaying social policy issues for the sake of emphasizing the budget deficit and arguing for the necessity of higher taxes.

But it is nonetheless important to ask how the Reagan administration has done on social policy matters, because the real effects of its early initiatives are only now beginning to emerge. Two of these initiatives are especially important. One was the series of federal budget cuts, organized by David Stockman and the Office of Management and Budget, that was enacted in the Omnibus Budget Reconciliation Act of 1981 (OBRA). The second was Ronald Reagan's proposal, outlined in his January 1982 State of the Union message, to "swap and turn back" federal programs. The essence of this plan was that responsibility for welfare (Aid to Families with Dependent Children and food stamps) would be turned over to the states, in exchange for which the federal government would assume responsibility for medicaid programs currently being run by the states. All of this was to be combined with an elaborate restructuring of taxes and grants.

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With respect to federalism, Reagan has been remarkably consistent over the years. As a conservative spokesman, as a governor, and twice as a presidential candidate, he has made much the same arguments, and urged much the same action, that he has from the White House. He has argued for a reduction in the role of the federal government in domestic programs in general, and for social programs in particular. He has sought to enhance the role of *states* (as opposed to localities, which Nixon and Ford favored in their efforts to decentralize). In addition, Reagan has been a forceful critic of federal welfare programs, for example Nixon's family assistance plan of the early 1970s. Specifically, he has criticized federal welfare programs that aid working-age, able-bodied adults; these, in his view, foster dependency on the federal government. All of these themes found expression in the OBRA legislation and in his "swap and turn back" initiative.

In assessing the outcome of these two efforts, the conventional wisdom holds that the Reagan administration was very successful in cutting domestic spending and shifting priorities to defense, but failed to obtain any real results on its federalism initiatives. In a word, we believe that this view is mistaken. In fact, the Reagan administration's domestic spending cuts, while significant in some areas, tend to be overrated in importance. And Reagan's federalism reform objectives, which are nearly forgotten in the public consciousness, now appear likely to have a substantial and lasting impact.

The states in a new light

Over the past three years, we have been conducting a national field network evaluation study of the Reagan administration's cuts and changes in federal grant-in-aid programs to state and local governments.[1] Our research, conducted by a group of economists and political scientists, focuses on the effects of these changes on state and local governments and the services they provide. Our sample includes 14 states, and 40 local governments within them. We have been conducting *longitudinal* research, which, it turns out, has been essential: The story of the effects of the Reagan cuts in federal aid has emerged only over time.

The 1981 budget reconciliation act was much more than a series of cuts in appropriations. It was, as reconciliation legislation has increasingly become, an important authorization law as well. It cut

[1] See Richard P. Nathan and Fred C. Doolittle, *The Consequences of Cuts: The Effects of the Reagan Domestic Program on State and Local Governments* (Princeton: Princeton Urban and Regional Research Center, 1983), and subsequent reports.

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funds for domestic programs (though not by as much as many people thought) by changing the rules of the game—eligibility requirements for entitlement programs, most notably. Moreover, the 1981 budget act also had important symbolic meaning: It signaled that the federal practice of "throwing money at problems" was ending. The companion Economic Recovery Tax Act of 1981 substantially cut federal revenues. All of these changes, as it turned out, put a spotlight on the states.

The changes in federal-aid spending levels under the Reagan administration are best understood if we divide them according to three main types of grant programs:

Entitlement programs like welfare, unemployment insurance, medicaid, and food stamps, in which the payment of benefits to families and individuals is administered by states and localities.

Operating programs under which the federal government provides grants to state and local governments for services like education, job training, public health, day care, and other social services.

Capital programs in which the federal government provides grants to states and localities for public facilities such as highways, mass transit systems, and waste water treatment plants.

The biggest cuts were made in *entitlement* programs—cuts that hit immediately and stayed in place. These cuts were largely confined to a particular group, the working poor. In the area of *operating* programs, large cuts were made in grants to states and localities for human-service programs, including public-service jobs under the Comprehensive Employment Training Act (CETA). But, as it turned out, carryovers from previous categorical aid programs partially cushioned the effect of some of these cuts. Moreover, some federal funds were restored in this area in order to combat the 1981-82 recession. The result has been a kind of plateau, and aid has not fallen to the levels contemplated at the time of the 1981 cuts. *Capital* programs were initially slated for large cuts, but by and large these failed to materialize or to be sustained. Even before the end of 1982, Congress was increasing funding in this area, and there have been large increases, for example, in federal aid for transportation facilities.

There is another important point to bear in mind. Historically, state and local governments have been very concerned about their finances in times of economic adversity. During recessions, they have battened down the hatches, cutting spending and raising taxes.

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This often amounts to an overreaction, such that when economic recovery occurs, many states and localities find themselves to be quite prosperous in new revenues, far in excess of their forecasts.

This pattern held, by and large, in the case of the 1981-82 recession, and state and local fears of the federal reductions further contributed to the typical belt-tightening. As a result, when the economy began to improve after 1982, states and localities were often in a good position to replace federal aid cuts with their own resources and to add new programs in areas where federal leadership and involvement were waning. And as we have noted, many of the operating program cuts, because of carryover funding, only began to take effect two or so years after they were enacted. They thus hit at what for many states and localities turned out to be a propitious time.

The origins of federal cost-cutting

Many observers have treated the administration's domestic policy initiatives as abrupt, discrete events, but those initiatives must be put in perspective. The retrenchment that they signaled at the national level has in fact been underway at other levels of government for some time. It began at the local level in the mid-1970s, largely as a response to the fiscal crisis in New York City. During those years, city governments began cutting spending and reducing employment—a pattern already well-entrenched when the new administration took office in 1981.

The turning point for the states was 1978, when Proposition 13 was enacted in California. Although other states had previously adopted limits on taxes and spending, Proposition 13 erupted like a volcano, spreading fiscal restraint throughout the country. Soon, the national government was affected; Jimmy Carter tried, with some success, to cut federal domestic spending in his last two years in office.

This pattern is demonstrated in the Table, which shows federal aid in real terms from 1978 to 1984, divided into three periods—the end of the Carter presidency, the Reagan initiatives in 1981, and the Reagan years after 1981. We have divided the grants into the categories mentioned earlier. The Table reveals a number of interesting points. First, the three-year reduction in the real value of operating grants at the end of the Carter administration was about the same size as the Reagan administration's reduction in 1981. It is important to note that, because the years between 1978 and 1981 were marked by increasing inflation, the unadjusted dollar-value of grants grew during those years. One must remember, however, that

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Federal Aid in Real Terms, 1978-1984
(In billions of 1978 dollars)[a]

Fiscal Year	*Total Outlays*	*Entitlements*	*Capital*	*Operating*
Carter Pulls Back Over Three Years, 1978-81				
1978	77.9	20.6	18.3	38.9
1981	73.1	23.9	17.0	32.1
Real Change	−4.8	+3.3	−1.3	−6.8
Percent Change	(−6%)	(+16%)	(−7%)	(−18%)
Reagan Makes Sharp Cuts in 1981				
1981	73.1	23.9	17.0	32.1
1982	64.1	22.7	14.9	26.5
Real Change	−9.0	−1.2	−2.1	−5.6
Percent Change	(−12%)	(−5%)	(−12%)	(−17%)
But then the Cutting Stops, 1982-84				
1982	64.1	22.7	14.9	26.5
1983	64.9	22.9	14.3	27.7
1984 (est.)	66.0	22.4	15.8	27.8
Real Change	+1.9	−.3	+.9	+1.3
Percent Change	(+3%)	(−1%)	(+6%)	(+5%)

[a] *Source:* Office of Management and Budget.

Carter also proposed a big-ticket "National Urban Program" in 1978, but the program went nowhere in Congress, largely because the administration could not sustain support for it in the aftermath of Proposition 13.

Qualifications also need to be noted about the Reagan administration's 1981 reduction in operating grants. Almost half of this 17 percent reduction in 1981-82 was due to the elimination of the public service jobs portion of the CETA program. By 1981, this program was exceedingly unpopular, and it would have been a prime candidate for the budgetary chopping-block even had Ted Kennedy or John Anderson been elected. Thus, it seems likely that the 17 percent reduction in those years was due less to the Reagan administration than to external forces that were already in place before the elections of 1980.

Overall, then, the Table shows that grant-in-aid spending (which had quintupled in real terms over the preceding two decades) began to fall off in the late 1970s; that the Reagan administration's actions in 1981 were consistent with this trend; and that the momentum for cutting domestic federal-aid spending has declined considerably since that year.

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Reagan's New Federalism

We return now to our main theme about the Reagan administration's initiatives toward a new federalism. If the administration did not get its swap/turnback plan through, just what did it end up with?

The task of isolating the changes produced by a particular factor, such as the federal aid policy changes under Reagan, is a difficult and challenging one. Nevertheless, there are clearly a number of Reagan changes that increased state influence. There were six newly authorized block grants in the 1981 reconciliation act that gave new scope for discretionary action to state government. A new Job Training Partnership Act (JTPA) also assigned the lead role to states. Moreover, a number of changes in medicaid enhanced the power of the states to cut and control the costs of this fast-growing program. Finally, as Nathan Glazer has argued in these pages, there has been a general shift in the behavior of the federal government, which now eschews laundry lists of new programs to solve domestic problems.[2]

The American federal system, of course, is diverse, intricate, and always changing. In several states in our sample, the role of state government was changing even before 1981. However, we are impressed, as we look across the 14 case studies for our study on fiscal year 1983, that the Reagan period has seen a resurgence in the role of state governments. The character and degree of this resurgence varies by state, but in a large and well-established political system such as ours, this shift is noticeable and important.

In large measure, the response of state governments to the Reagan program consisted of actions taken to avoid or compensate for what otherwise would have been (or it was feared would have been) the effects of the Reagan cuts and changes. These reactions have created the appearance of stability, but they do constitute change. States reshaped programs to reflect state priorities; increased their financing of some programs in which the federal government has become less active; and assumed more control over the activities of local governments and nonprofit organizations that receive federal funds. In all of these ways, as well as in others, states increased their influence relative both to the federal government and to local governments and nonprofit organizations.

All 14 states in the sample for our study responded to the opportunities for a greater role, though in different measure and in different ways. Eight states made what we consider a pronounced response

[2] "The Social Policy of the Reagan Administration—A Review," *The Public Interest* 75 (Spring 1984).

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to the opportunities for increased influence created by the Reagan administration's federal aid policy changes. Three states (Massachusetts, New York, and, to some extent, New Jersey) supported many of the federal programs that were cut or would have been affected by the Reagan proposals and had the fiscal resources to fill the vacuum that the cuts created. Arizona and Florida—both conservative, fast-growing states—had governors who supported Reagan's decentralization objectives, and both states acted in several areas to take advantage of these changes. Three states (Missouri, Ohio, and Washington) faced severe fiscal conditions and viewed the New Federalism as an opportunity to confront them. Key points from the reports on some of these states are presented below.

Massachusetts. Our field research associates for Massachusetts report that the "state government's decision-making authority and administrative responsibility have increased significantly in most of the operating programs studied." The new block grants created under OBRA in 1981 are the most important example. The associates report that the block grants increased the state's influence over programs in many areas, and that "local governments must now orient their policy processes at least somewhat more to take account of the state's preferences." Reflecting its support for the purposes served by federal programs, Massachusetts has used the new block grant authority primarily to maintain services by shifting funds and replacing federal cuts. The capital programs present a slightly different situation. Although the state's authority over capital programs has not increased formally, the fact that this state government has chosen to replace substantial portions of federal cuts (and threatened cuts) has increased the state's influence with local governments and special-purpose regional bodies. Under medicaid, the state has developed an annual cost saving agenda, including the establishment of a "managed-care" system for medicaid and an experimental hospital reimbursement plan.

New York. Our field research associates for New York report that "the Reagan program has been accompanied by a greater centralization of policymaking and financing at the state level." They emphasize that the state's political culture and history were important determinants in its response to the administration's changes. "The legacy of the reconciliation act is important to note—not so much for its ability to reorder intergovernmental relationships within New York—but rather for its ability to reinforce those characteristics of big government and liberalism that make New York unique." For the state government, the major institutional changes

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involved its role under the block grants and the new Job Training Partnership Act. Like Massachusetts, New York State moved to protect services under the six new block grant programs. Under medicaid, the New York associates report that the Reagan initiatives "served indirectly as a catalyst for the implementation of substantial changes in the fiscal management of medicaid long under discussion in the legislature." The state's overall financing role increased during the Reagan years, continuing a trend begun in the mid-1970s. This is seen in the increased state funding of medicaid, the replacement of reduced federal funds in block grant programs, and increases in state funding for highway, mass transit, and housing programs.

New Jersey. The New Jersey associates report that the state government's role in program administration has been strengthened in the Reagan period, most notably in the new job training program, although increases occurred in other areas as well. The associates cite new policies under medicaid and direct state administration of the block grants as evidence of a more prominent state role. They also report that federal changes affected the state's role in financing capital programs: "Proposals to establish an infrastructure bank, efforts to create stable sources of state transportation aid, and the merger of the state's two housing agencies were attributed, at least in part, to federal aid changes."

Arizona. The Arizona associates report that the Reagan domestic program "enhanced, and in some cases speeded up state and local actions and responses" that were reshaping the state's intergovernmental organization. The block grants were viewed as important, "obviously strengthening the hand of state government in general, and the state executive in particular." Governor Bruce Babbitt saw the new block grants "as an important political and economic resource" and moved quickly to implement them. The governor also saw the new job training program as "an opportunity to bring the state into an area previously left to local discretion." The changes in health care for the poor made for the most dramatic shift. Arizona's entrance into the medicaid program shifted primary responsibility for indigent health care from a county hospital system to a new statewide medicaid program. The transition, however, was not without its stresses and strains. With the failure of private administration of the system, the state is now directly involved in administering this program.

Washington. The Reagan 1981 changes in federal aid came soon after state officials in Washington had determined that a sudden reversal in the state's economic fortunes required a major cut in

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state spending. Our associates report that, "while there is no doubt that the Reagan program strengthened the relative role of state government . . . , the reductions and administrative changes initiated by the Reagan administration should be seen as validating a trend in Washington already underway in early 1980." This greater state role occurred, according to the associates, "through a greater concentration of managerial responsibility at the state level, more monitoring accountability, and increased state control over the distribution of funds." The state's response has been clearest in its implementation of the block grants. State officials took the lead in fashioning a coordinated response to many of the new block grants: They proposed cutting low-priority programs, shifting funds to protect others, and redistributing aid from large cities to the rest of the state. Under the new job training program, the state now requires detailed plans from local service providers. As in other states, the governor has taken steps to integrate this program with the state's economic development activities. Under medicaid, the severe fiscal pressures on the state government have forced the state to make cuts in services and limit eligibility.

For the other states in the sample, the case-study reports by our field researchers for fiscal year 1983 show similar, though generally less pronounced, tendencies for the state to take on a stronger role. Again, the block grants, the new job training program, medicaid, and the overall effect of federal government retrenchment in domestic areas were cited as major reasons for, and indications of, this shift. In many cases, this shift built on trends already in place before 1981—as, for example, in the case of state efforts to play a stronger role in health financing in order to get control over burgeoning medicaid costs.

In addition to the enhanced state role *vis-à-vis* Washington, which we have emphasized, a similar increase appears in the state role *vis-à-vis* local governments. Because local governments are now more dependent on their states, the states can play a larger policy role in areas such as health financing and job training, and in the programs affected by Reagan's new block grants.

One finds a similar shift in the role and importance of nonprofit groups, especially those that provide social services. With the exception of food programs for the hungry, these groups (many of them throwbacks to Lyndon Johnson's War on Poverty) appear to be losing out to the states. A major reason for this is the elimination of CETA public service job funds, which provided important fiscal support for these organizations in the mid- and late 1970s. Nonprofit social

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organizations have also lost out under the administration's block grant that assigns the authority and money for community action agencies (linchpins of the Great Society) to state governments. Previously, these agencies received direct grants from Washington. The same is true of nonprofit agencies that provide public health services, notably community mental health and local public health clinics—they have lost out under the new block grants in the health field.

A sleeper issue

Taken together, these structural changes in federal-state relations, state-local relations, and in the role of nonprofit organizations affect a broad gamut of programs and agencies in the domestic public sector. It is unlikely that these changes are just temporary adjustments, easily reversible in subsequent years. This is where the big 1981 tax cuts enter the picture. Even if federal officials for domestic programs did attempt to reverse course and return to the "good old days," the federal deficits would cut them off at the pocketbook. Unless federal taxes are raised well above the level necessary to close the budget gap, which seems unlikely, the federal government does not have the fiscal flexibility to reverse this flow of influence and responsibility to the states.

Writing at the end of World War II, the economist James A. Maxwell made a prediction about the relative roles of the federal and state governments in American federalism: "If the public demand for governmental services continues to grow, the state governments will soon appear to have more duties than they can handle effectively, and federal intervention will be indicated." Maxwell, of course, was right. But we think that there has now been another basic shift. The federal government is pulling away from domestic social programs, and national leaders have been slow to pick up on the significance of these changes. Ronald Reagan's "New Federalism" may turn out to be the major sleeper issue of his presidency.

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EDITORS' NOTE: Due to an editorial error, information was omitted from the contributor's note on Stephen Rosen, author of "Systems Analysis and the Quest for Rational Defense" in our last number. Mr. Rosen is a member of the National Security Council Staff. The views expressed in his article are his own, and do not necessarily reflect those of the U.S. government. We apologize for this error.

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FALL BOOKS

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Growing into Democracy

ANDY STARK

John Lukacs: **Outgrowing Democracy: A History of the United States in the Twentieth Century.** ***Doubleday. 480 pp. $19.95.***

JOHN LUKACS'S *Outgrowing Democracy* is about the decline of America in her second century. The evidence marshalled is familiar enough: The quality of education is flagging; productivity is on the wane; the foreign policy establishment does not understand the Soviets; bourgeois urbanity—the fine edge at which the middle class meets high culture—has vanished; bureaucracy is ever more paralytic; and so on. Much of *Outgrowing Democracy* suffers from the flaw that habitually plagues American jeremiads: Its idiosyncratically chosen evidence cannot sustain its overdrawn conclusions. In *The Culture of Narcissism*, Christopher Lasch—one of Lukacs's colleagues in this genre—thinks the title of the soap opera "One Life to Live" is evidence of a new American preoccupation with the present at the expense of posterity. (Reading this, one wonders whether Lasch would now concede that the release of the James Bond film "You Only Live Twice" signals a renascent concern for the American future.) Similarly, at one point in *Outgrowing Democracy*, a darkly cynical remark by Norman Rockwell about one of his most wholesome paintings is taken as a sign of the deep skepticism that lies just beneath the surface of American optimism. Presumably, however, Lukacs's own earlier observation that there "are now people in this country who think it is cold because the radio says it is" could easily stand as evidence to the contrary—namely, of the credulity that lies behind American pessimism. Perhaps that is why he buried this observation in a footnote.

Although much of the book cannot be taken seriously, one of its themes deserves to be taken very seriously indeed as a problem in political philosophy. "In one important sense," Lukacs writes, "most [19th century] critics of popular democracy missed an essential point. What loomed ahead was not the rule of the mob, it was the manipulation of the masses by the politicians." This thesis rests on the distinction Lukacs draws throughout the book between "public opinion" and "popular will." In the 19th century, "public opinion" referred to the "opinion of the more or less educated classes," whereas "popular will" denoted the "unenlightened sentiments of the masses." It is a distinction that survives into the 20th century.

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But now, Lukacs insists, the poles are reversed. Today it is the masses who embody "public opinion," and the educated elite who control or minister to "popularity." On the one hand, as the populace grew more educated, "public opinion" became "no longer synonymous with an educated class; it was less and less separable from the people." On the other hand, a "public relations" elite has evolved, an elite whose goal it is to replace "verbal politics" and reasoned consideration in political debate with the manipulation of images and repetition of slogans integral to popular appeal.

Unfortunately, Lukacs argues, this transfer of political rationality, from a "public opinion" elite to the people, has been accompanied by a transfer of power from the people to the "public relations" elite. In the 19th century, it was the irrational majority that was "powerful" and "tyrannical"; the intelligent public opinion elite, according to Samuel Butler, was generally impotent and cowed. Today, however, it is the "public relations" elite that is "insistent, influential, and powerful," while the majority is "silent, passive, [and] acquiescent." In sum, though it keeps changing, the locus of power in American democracy has never been the epicenter of intelligence.

TRADITIONALLY, the attempt to distinguish between "public opinion" and "popular will" has necessitated a search for a meaning of "public" that is not simply a synonym for "popular" or "people." Frequently, the difference between the two is interpreted as that between an "organized community on the one hand and the mass or crowd on the other." Robert Nisbet, who wrote those words, continues:

> What proves to be public opinion in a community is commonly generated by popular opinion, whether in majority or minority form, but it is only through a process of adaptation or assimilation—by the habits, values, conventions, and codes which form the fabric of the political community—that popular opinion ever becomes what we are entitled to call public opinion . . . .

It is, generally, a particular sort of thinker who wants to distinguish public opinion from the will of the people. He is usually skeptical that the democratic "masses" or "crowd," of themselves, will naturally issue forth with intelligent political decisions, but he is equally uncomfortable with entrusting the management of government to an intelligent elite too far removed from the people. The idea of a "community" or "public" distinct from the "masses" or "people" appeals to such ambivalence. For into it can be read both the democratic sanction of numbers (since community is but a higher-order refinement of "people") *and* the intellectual credibility of wise habit and convention (since community also entails shared codes and values). In "public opinion" they have found a place in democratic politics where rule-by-number and intelligent government somehow embrace.

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One is tempted to be suspicious of a device whereby the profoundly ambivalent suddenly resolve their concerns. If the problem is that the people, on the one hand, and their wisdom-bearing habits, codes, conventions, and values on the other, are frequently found apart or at odds, then how can they be reconciled merely by the creation of a meta-concept like "community"? If "public opinion" is derived, or "generated," in Nisbet's words, from "popular will," then "public opinion" is really no more than the will of the people improperly garbed in the trappings of credibility that come from the claim to speak with communal wisdom. "Public opinion" is but a more dangerous, because more respectable, version of "popular will." If, on the other hand, "public opinion" arises from a certain elite, then its wisdom is illegitimately empowered by the sanction of numbers that comes from the claim to speak for the public. Presented as "public opinion," its assertions seem much more incontrovertible. And, in such proclamations of "public opinion," the real problem remains unsolved: that of reconciling democracy with intelligent government, or power with reason.

"THE EVERLASTING QUESTION of philosophical politics," Lionel Trilling once wrote, "is how to place reason and power in the same agent." This is clearly Lukacs's overriding concern—the reason embodied in "public opinion" and the power of commanding "popular" approval seem never to go hand in hand in American democracy. Yet Lukacs's terms lead his analysis away from the real problem. The question of public opinion should really not so much be a question of "public" as of "opinion." It is not a social question —of community, mass, and elite—but the political one of government and governed. The Founders were relatively untroubled by the concept "We, the People"; they spilt their ink to ensure that the political system issued forth in, and then empowered, the most intelligent opinion on a given issue. They were concerned, in the words of *The Federalist*, that government "refine and enlarge the public views, by passing them through the medium of a chosen body of citizens, whose wisdom may best discern the true interest of their country."

To the Founders, the important distinction was not between public opinion and popular will, but between public interest and private interest; not between two ways of conceiving the corporate body, but between two ways in which an individual might conceive a political opinion. The democratic citizen, the Founders recognized, could not be expected to think reasonably, clearly, and synthetically about all intricate affairs of state. The Founders' response was to offer political "representation" instead of pure democracy, not to pit the "public" against the "people." It was their aim to design a government that would resolve Trilling's "everlasting question," a government in which the purest of political reason would be filtered to the apex of power.

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Following the Founders, many American democratic theorists of the century under Lukacs's analysis—our own century—have eschewed his public-versus-popular idiom, and, consequently, have not despaired of reconciling reason and power. Schumpeter's concern, for example, was with representation versus democracy, not public opinion versus popular will. Indeed, he saw no meaningful distinction between "common will" and "public opinion," but instead asked to what extent the private citizen can be expected to think, always and completely, in the public interest. His concern was not that the average citizen has no communal or historic ties, but that the opinion-making apparatus in the individual mind is sometimes problematic for politics; his focus was on "opinion," not "public." Ingeniously, if somewhat counterintuitively, Schumpeter urged that the issues we care most about—personal matters—we tend to decide calmly and rationally, because we take the time to explore them, and we feel directly responsible for their outcomes. More distant issues, such as those of state, we tend to approach imagistically, emotionally, carelessly, irrationally; hence, political reason is most frequently to be found not in the *demos*, but in representatives. Democratic opinion-making is, and should be, merely reflected in voting; elite or expert opinion-making should reside in representative government. In this way, reason and power are maximally combined in democracy.

Similarly, Walter Lippmann wrote:

> Because of the discrepancy between The People as voters and *The People* as the corporate nation, the voters have no title to consider themselves as proprietors of the commonwealth and to claim that their interests are identical with the public interest.

If he seems to be distinguishing between public opinion and the popular will, the broader context of *The Public Philosophy* reveals that Lippmann's concern was really that many public policy issues are simply too detailed, complex, or long-run, for private citizens to deal with intelligently. They are to vote, and then to allow their representatives, under watchful eyes, to carry on the nation's business. It is, for Lippmann, the voters who cannot always speak about politics, not the people who cannot always speak for the public.

THOSE WHO DISTINGUISH "public opinion" from "popular will" without considering the representative democratic institutions designed by the Founders will never reconcile reason and power, or intelligence and numbers, in politics. Lukacs contrasts "public opinion" and "popular will" throughout *Outgrowing Democracy*; Madison is mentioned once, Hamilton never makes an appearance, and *The Federalist* crops up only twice in this treatise on American democracy. Lukacs might argue that the Founders designed representative institutions that, in America's first century, transferred some power from an irrational popular majority to a reasonable public-opinion elite; but that such institutions are inappropriate now that

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the majority is reasonable and wise, and the elite is infantile and superficial. In that case, though, the implication of Lukacs's argument is that we have outgrown representation, not democracy; indeed, that we should be growing *into* democracy.

There is another strand of democratic thought that Lukacs does not consider. Suppose he is right—and he would not be alone—in arguing that reason and power have never coalesced in American politics; that the representative institutions of the Founders did not work in the 19th century, and are outdated in the 20th century. The prior question, even prior to Trilling's, is whether the relative separation of reason and power is such a bad thing in democratic societies. Perhaps their separation is one of democracy's virtues, not one of its vices. Such, anyway, was the view of both Burke and Mill.

For all their faith in the representative's ability to effect such a political reconciliation, Burke and Mill did agree that reason and power are not often found together in society. They concluded thus, not on the grounds that power corrupts reason, and reason is too unworldly for power, but rather on psychological grounds: Power in politics, they saw, is too closed-minded and zealous for reason, and reason is too tentative and diffident for power. Psychologically, it has *always* been the case that the reasonable lack all conviction, and the irrational are full of passionate intensity. Mill distinguished between the "capacious and impartial" rational mind and the "energetic," "one-sided" mind of the zealot; since, clearly, no single mind can be impartial and one-sided at the same time, reason and power are rarely found in the same person. For Burke, when an idea—say Jacobinism—takes the form of an "empire of light and reason," its propounders will be of "cold heart"; when an idea—say atheism—takes a form "against our reason," its propagators are said to be buoyed by a "hot spirit drawn out of the alembick of hell."

Both Burke and Mill believed that neither the reasonable nor the zealous have a monopoly on truth; reason and zeal are both sometimes right, sometimes wrong. Consequently, their mutual exclusivity has its advantages. For Mill, the reasonable and the zealous engage in a political debate that ferrets out the truth. If the zealous are arguing error, Mill writes, this will serve only to sharpen the truth in the eyes of the reasonable; if the one-sided are forcing the truth, the reasonable open mind will eventually be impressed by it, and trade in its error. For Burke, it is the competition between the reasonable and the zealous that mitigates error: Since reason can easily take the side of error, we ought not lament its separation from power; since power may equally err, it is perhaps a blessing that it is generally denied the additional weapon of reason. Of this Burkean strand in England, Paine wrote: "In this way [the citizen] is on his guard against political theories and adventures; the constitution does not fall into the hands of theorists, nor its business into those of hotheads."

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IN AMERICAN DEMOCRACY, as Lukacs suggests, there has been at best an uneasy relationship between reason and power. The slogans associated with the 1964 presidential candidates—"Extremism in the defense of liberty is no vice" and "Come, let us reason together"—could not have been the utterances of one and the same "agent." That we are likely to find something sympathetic and credible in both Barry Goldwater's plea for one-sided extremism in the defense of a mainstream idea, and Lyndon Johnson's bid for reason as the ideal faculty to consider and reconcile extreme alternatives, suggests how highly both reason and zeal are esteemed in American politics.

The history of American reform is, in part, the story of the interaction of reason and zeal, a story both Mill and Burke would have understood. This strand of American history escapes Lukacs, perhaps because his approach is so different from that of the 19th-century thinkers he criticizes. Lukacs' perspective is not that of a traditional democratic theorist, but of a certain sort of apolitical moral philosopher. For such moral philosophers, reason is held to be radically opposed to passion, as if they are two cohabiting and competing entities in the soul—of which one or the other, usually reason, is held morally superior. For the democratic political theorist, the problem is just the opposite—reason and power rarely coexist in the same "agent" at any one time: They are incompatible. But each has an equal moral claim, and each is instrumental in preserving or reaching the truth. Lukacs's view that America has outgrown democracy shows him to be one who believes, as Trilling wrote of Matthew Arnold, "so firmly in reason that he was certain it justified the use of its antithesis, force, without which it was powerless." It is because Lukacs writes in an inappropriate idiom that he does not consider the degree to which reason and power may be combined in the representative institutions of American democracy, and the degree to which the relative separation of reason and power might in fact be one of democracy's cardinal virtues.

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Every Man a Patron

RONALD BERMAN

Edward C. Banfield: **The Democratic Muse: Visual Arts and the Public Interest.** *Basic Books. 256 pp. $15.95*

EDWARD BANFIELD'S *The Democratic Muse* will be the subject of a great deal of criticism, some of which it frankly arouses, and one should begin by placing it in context. It is one of a number of

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recent books that have responded to government patronage of culture. These books are not confined to the American scene: They include Harold Baldry's *The Case for the Arts* which studies state patronage in England, and Elizabeth Sweeting's edition of *Patron or Paymaster?* which does the same for Hong Kong and Malaysia, as well as Canada and France. (For the United States Dick Netzer's *The Subsidized Muse* should be added to the list.) Such books make up a small and valuable library on a new subject. They have different points of view, but they address themselves to the issue in a much more than political way: That is to say, they are not satisfied with the appropriation of funds to solve cultural "problems." It might even be said that they view the problems to arise *from* the appropriation of funds.

Banfield's book is about the following subjects: various definitions of artistic purpose and activity; the legislative and political histories of the National Endowment for the Arts; the administration of that agency; the operation and *raison d'être* of public museums; the costs and benefits of teaching art in schools; the economic ethics—or at least the value—of exhibiting and collecting original works of art as opposed to copies; fine arts and crafts; art as a form of welfare; and art as a public interest.

But *The Democratic Muse* is considerably more than a study of aesthetic crimes, vices, and follies. One of the problems of other books dealing with government patronage is that they do not concern themselves with important theoretical issues. They deal with grants and their consequences. This book is remorselessly theoretical: It deals with artistic definition, quality, and values. Government patronage of art is in a sense invulnerable to political discussion —what matters, after all, is that funds be distributed to constituencies. Very rarely are distinctions made between the ideal and actual uses of such funds, and almost never are the works or services that are made possible by such funds subject to evaluation. In fact, as Banfield often points out, it is anathema to do so: Nothing could be less useful than for a government agency like the National Endowment for the Arts to make distinctions in quality between its grantees. Mythologically, which is to say politically, all grantees are equal. But the issues raised by Banfield have to do with the public effectiveness of subsidy; with alternatives to subsidy; and with the evaluation of subsidized works.

BANFIELD BEGINS with the consideration of what art is or may be. It is a useful discussion and, speaking of crimes, vices, and follies, it is a treasure trove of future quotations. Everything is there, from the skinned rabbit recently hung (literally) at the Art Institute of Chicago, to the project submitted to NEA which would make taxidermy a branch of sculpture. Banfield's discussion of aesthetics might be assisted by a somewhat larger contextual discussion: Since

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Marx has become a university totem, another variable has been added to "culture." That, of course, is criticism. The art world's profound determination to avoid evaluation of art objects, to identify and praise only the intention or the artist of even the "creativity" of his aspiring audience, has been legitimized and even graced by a sequence of theories. In art, in literature, and in other cultural modes, we now find that there are no intrinsic differences in constructs. The study of texts has become the study of "discourse"—and to discourse, the television commercial or the restaurant menu are the same as Shakespeare. They are instrumental in revealing the intentions of the artist, conscious or not, and, even more important, in revealing the dead weight of capitalist culture on his sensibility.

Robert Alter has put the matter briefly in the March 1984 issue of *Commentary*: "Why, indeed, undertake a 'reading' of *Anna Karenina* when your intellectual responsibility is to unmask its pretense to represent reality, to show how its notions of causality and personality and psychology merely replicate the arbitrary and coercive values that govern society as a whole?" Why, indeed, undertake to justify funding certain works of art because they are important or beautiful (terms now not likely to be invoked) when we know that all forms of art are equal?

Arguments about elitism versus populism are probably short of the mark. We are now at a convergence of democratic political history and Marxian critical theory, at least in the microcosm of artistic subsidy. The natural reluctance of democratic government to make distinctions between voting beneficiaries results in the pretense that the equal distribution of benefits matters more than the invidious comparison of results. And the intellectual background of politics provides politics—and universities and media—with the fortunate idea that this is perfectly justifiable. Possibly the most interesting thing that can be said about intellectual response to government patronage is that it has not been in opposition. It has assented silently to the assumption that art is inherently the realm not of distinctiveness, but of equality.

POSSIBLY, as Banfield suggests, this has been a matter of agreement. Strategic silence, even the invocation of self-censorship, accompanies the infinitely widespread distribution of patronage. As a consequence, the funding of many useless things allows the funding of some important things. As Banfield sees it, the academic world has silently assented to the system of feeding the sparrows by feeding the horses. But we might also think of government patronage as part of the new intellectual dispensation. There have been many studies of bureaucracy, but few of bureaucrats. My sense of it is that bureaucrats of culture sincerely do believe that art is a matter of intention. They may not all be populists, but a certain number of them are structuralists. Cultural bureaucrats assume that the mak-

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ing of distinctions between works of art is a lost bourgeois illusion. They are much irritated by the imposition of interpretation. So far as they are concerned, what matters is the purpose served by art, not works of art in themselves. This accounts for the published statements of governmental patronage such as the annual reports of NEA, and offers a bit of insight into human character at the present time, which hungers after artistic identity. Some years ago the phrase was that we are all guilty. For now, we are all artists.

One of the best things about *The Democratic Muse* is its coverage of what might be called patronage theory. I believe that the most common justifications for government support of art are couched in the language of social benefits. Art and its patronage provide us with better people and better cities. Art is a source of higher morality. It is a form of secular religion. It may even be a necessary form of therapy. Yet the patrons who confer these benefits do not have to account for aesthetic choice. Banfield's concern is to show to what extent the social benefits of government patronage are unexamined or misinterpreted. He adduces enough aesthetic history to put the theory of social benefits in doubt, and he has examined enough cases to separate failure from success. After this book it will be much harder simply to assume that art has inherent and direct social value, or that the patronage of art can be free of aesthetic evaluation.

There are some lovely arguments dealing with NEA legislation and with the enthusiastic support it has aroused among constituencies. Here is Banfield examining the unexamined:

> Some of the most frequently and earnestly made arguments rested on grounds that are, to put it generously, insubstantial. It was highly implausible . . . that "giving official recognition," as by the establishment of an advisory council, would "give status and recognition to the importance of culture in the United States," increase "national prestige," contribute to international understanding and world peace by enabling other nations "to discover that America has a soul," and bring the ghettos of the cities into "the mainstream of American culture." What exactly is national prestige? How is it measured? Why should Americans want more of it? (After the Revolutionary War, according to historian Neil Harris, art was seen as a means of convincing skeptical foreigners of the existence of an American nation. By now, it is safe to say, they have been fully convinced.)

These are what have been traditionally described as inconvenient questions, and Banfield asks a great many of them.

SO FAR, very little of what any reviewer could discern would seem to cause problems for the reception of the book. The critique it makes affects an establishment, but that critique is made in so logical and elegant a way, and is based so firmly on scholarship, that it would seem best for its adversaries to measure their own arguments by its standards. Once the matter comes into the open, it is very difficult to defend the second-rate by arguing that people like it, or

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that it provides contingent social benefits. And it will now be harder to defend grants like the one that proposed to take a pig, two female rabbits, a buck, two ring-necked doves, a monkey and the artist on a tour by motorbike, "with a large sidecar."

The problem caused by *The Democratic Muse* is that it is also critical of success, intellectual and aesthetic. This is how Banfield puts the matter: "If it were clear that art significantly affects the quality of society, as opposed to the welfare of individuals, it would not follow that government might properly subsidize it or otherwise intervene in art matters. There are many things that affect society in ways that ennoble or debase men, ways that by common agreement are not the concern of government, either because it is incapable of managing them . . . or because it is understood that government exists for other purposes." Even if the patronage of art worked, Banfield would be against it on constitutional grounds.

A large section of *The Democratic Muse* applies a constitutional as well as a common-sense argument to art patronage. And it debates the effects of that patronage not at their most extreme, but in their most conventional forms. Banfield, for example, is against the teaching of the visual arts in schools, against collecting fine arts for the exhibition of original works to the public, and against museum subsidies of most kinds. His position is that museums already receive a number of benefits from government, chief among them tax-exempt status. He views museums as displays of what wealth has not always wisely collected. Their holdings are in fact termed "collectibles" in *The Democratic Muse*, not art, because they are characteristically (and only) rare and costly. His case against the museum, then, is that it exhibits private taste, exempts this taste from taxation, and calls the result public welfare.

There are a number of subsidiary issues: The museum, as Banfield sees it, accepts gifts not because they are aesthetically meaningful but because not to do so would offend potential donors of funds. It tends naturally to exhibit what matters only to those donors, and to critics and sympathetic media. Finally, it pretends to serve useful social purposes, such as the education of school children, with no real conception of either function or result. One is reminded of Samuel Butler's case against leaving money to universities: "What a beast a man must be too who leaves his money in this way. I wonder he is not ashamed to tell the world that he has died without having seen one person whom he has loved well enough to let him have his money when he can no longer use it himself." Both Butler and Banfield have a good deal of reason and justice—but not all of either.

BANFIELD SPENDS considerable time on one thesis that is bound to expose *The Democratic Muse* to attack: Museums should exhibit copies and reproductions instead of originals. He believes that tech-

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nology can now duplicate almost anything so closely as to confuse even expert critics. This represents an opportunity for museums to rid themselves of vices: to pay only nominal sums for "masterpieces"; to cease the inflation, both economic and moral, of art culture; to make possible, finally, the widest public access to works of art. The idea is fascinating. Clearly, certain art forms are duplicable. The works of Degas and Rodin, of all sculptors who use the casting process, are essentially sequences of originals. It would be splendid for every museum in America to have a Rodin. So far as sculpture from castings is concerned, the cost of acquisition would drop while the criterion of rarity (Banfield calls this "the cult of the original") would come to matter less. The idea could be extended to minimalist painting since there is not much difficulty in duplicating dots, lines, or spaces. And of course, in a sense, Banfield has been preceded by Warhol, whose work argues against pretension. But there are insuperable problems, and the inclusion of this argument in *The Democratic Muse* will make it harder for the rest of the book to have its effect.

The first argument is simply economic: Artists are entrepreneurs and can decide whether to market prints or limit production to single canvases. And today they also have copyrights. The museum can only acquire what is available. If artists and dealers agree that work should be confined to single originals then there is not much the competing purchasers can do. They can opt out of the market, but they cannot increase the supply. Second, and more hypothetically, I believe that rarity does constitute part of the value of art. But no matter—the important thing is that rarity constitutes part of mass expectations. If all museums were now empty, and if we started off from ground zero, it might be possible to encourage the public to allow its institutions to acquire duplicate sets of all known originals. But the three or more thousand museums in this country now have an almost unimaginable investment in the rarity of their holdings. To ask them to give that up makes as much sense as asking stamp collectors to give up the "artificial" value of their own rarities. No one wants a major investment to become a three-cent stamp.

I HOPE that readers of *The Democratic Muse* will concentrate on its indisputable virtues. Banfield has done for culture what Milton Friedman has elsewhere done for industry: He has given us a realistic picture of a market shaped and distorted by intervention. Friedman calls the relationship of legislators, bureaucrats, and beneficiaries "the iron triangle." Friedman's example is the tobacco industry, Banfield's is the culture industry. Both show, with remarkable persuasiveness, how congressional committees become involved not with the *rights* of the interests they oversee but with their *success*. Legislation nearly always begins by addressing an inequity or a problem of some kind, and nearly always ends by eternalizing a subsidy. The importance of *The Democratic Muse* lies in its recogni-

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tion that culture more and more assumes the proportions of an inefficient, protected industry.

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Class Conflict over Civil Liberties

JEREMY RABKIN

Norman Dorsen, ed.: **Our Endangered Rights: The ACLU Report on Civil Liberties Today.** *Pantheon. 333 pp. $11.95.*

Herbert McCloskey and Alida Brill: **Dimensions of Tolerance: What Americans Believe about Civil Liberties.** *Russell Sage Foundation. 512 pp. $29.95.*

THESE TWO BOOKS scrutinize the edifice reared by contemporary liberalism in the name of "civil liberties"—and find it quite intact. Neither volume ventures any serious analysis of the rather extreme constitutional doctrines they embrace. Each calls attention to some interesting ideological affinities and sociological correlations in the patterns of support for these doctrines, but neither set of authors is seriously interested in pursuing the implications of these patterns. Still, both books do inadvertently suggest several reasons why the civil libertarianism of the recent past may indeed prove very vulnerable to the changing mood of national politics.

The ACLU volume is a follow-up to an earlier survey of this kind, produced by the ACLU in 1970. The earlier book had a more candid title: *The Rights of Americans: What They Are, What They Should Be.* The title of the current volume is a fair measure of the ACLU's progress since then. Several items from its 1970 wish list are here presented as revered elements of our national heritage, by now too clear to be disputed. But, for the most part, the individual essays in this volume do not reflect the alarmist note in the title. Near the end of the book, Norman Redlich's essay on "Religious Liberty" finds sinister implications in the "religious crusade" of the Moral Majority, while Morton Halperin finds ominous threats to privacy and the free flow of information in the Reagan administration's approach to national security. But most of the other essays are already looking ahead to new issues, new fields to conquer in the name of "civil liberties."

Indeed, the most revealing thing in this book is the extraordinary scope the ACLU now gives to the term civil liberty. The bulk

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of the essays are gathered in the middle section, candidly headed "The Rights of Groups." Here we find pleas for prison reform and for new programs to enhance racial integration. But there is also an essay on "Justice for Aliens," calling for a more sympathetic government posture toward refugees and illegal aliens, and an essay on "Sexual Justice," demanding special protection for homosexuals, legal recognition of homosexual marriages, and the rejection of any distinctions between men and women in the military. Then there is a neo-Marxist essay on "Economic Justice," demanding income redistribution and social control of corporate investment—in the name of enhancing liberty. On the other hand, freedom of speech and freedom of the press, which most people regard as core elements of civil liberty, receive no separate or sustained discussion at all in this volume. Instead, there are essays such as the one by Thomas Emerson on academic freedom, in which he endorses court challenges to the adoption of "racist " school texts, while simultaneously endorsing court review of the "censorship" involved in removing inflammatory books from school libraries.

BY CONTRAST with the ACLU volume, *Dimensions of Tolerance* keeps its advocacy to a minimum, generally maintaining the detached tone of social science. The book reports and analyzes results of extensive public opinion surveys conducted during the late 1970s on questions relating to civil liberties. Its principal finding is that the general public is substantially less committed to "civil liberties" than various elites are. To their credit, it must be said, McCloskey and Brill do not take an alarmist view of this finding. They simply conclude that most people have not been as fully exposed to, or as well informed about, civil libertarian norms as the more educated elites.

This explanation probably has more to it than the authors realize. They conclude, for example, that "the public often lags far behind . . . in its tolerance toward freedom of the press" because 55 percent of their "mass public" respondents agreed with the proposition that, "To protect its moral values, a society sometimes has to forbid certain things from being published." Meanwhile, in a separate survey of "opinion leaders," the authors tell us, 51 percent rejected this proposition in favor of the view that, "Nobody has the right to decide what should or should not be published." It is inconceivable, however, that a majority of "opinion leaders" are opposed to restraints on the most vicious and lurid child pornography, as even quite liberal courts have endorsed restraints in such cases. Almost certainly, then, the elite respondents were simply nodding at a platitude or recoiling from the code words "moral values" in the alternative proposition. The mass public, less sensitive to the approved postures and respectable formulas of civil libertarian discourse, presumably did think of such particulars and gave a more commonsensical response.

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One can, in this way, question the reliability or the meaning of many other survey responses reported in *Dimensions of Tolerance*. And one can certainly take issue with the authors unrelenting identification of "tolerance" or "support for civil liberties" with the permissive or non-interventionist response—whether the question involves desecrations of the flag, homosexual activists in the classroom, or racist tirades on television. Nor do the authors probe very deeply into the consistency or sincerity of their civil libertarian respondents. Their questionnaires, for example, make no effort to explore the correlation between "libertarian" responses on domestic issues and indulgent attitudes toward left-wing dictatorships in other countries. (The ACLU volume, for example, includes an essay by Aryeh Neier on "International Human Rights" that scolds the Reagan administration at great length for its policies in Central America, and says not a word about human rights in Cuba or indeed in the Soviet Union.) Similarly, the authors do not think to question their "civil libertarian" respondents on what should be done when student protestors prevent government officials from being heard on campus. (The ACLU volume also ignores this timely issue entirely, even in its discussion of "academic freedom.")

But such objections are doubtless beside the point. *Dimensions of Tolerance* does about as well as one can expect from a study of this kind: It supplies an aura of specious precision to its labored demonstration of the obvious. Thus McCloskey and Brill find that those who take the most extreme positions in favor of free expression and freedom of lifestyle also tend to be the following: well-educated professionals; self-described liberals; strong advocates of equality, of business regulation, and of income redistribution; also, proponents of social change who believe in "putting their faith in theories, plans, programs and [in] 'thinking' people 'who have lots of ideas.'" On the other hand, McCloskey and Brill tell us, these strong "civil libertarians" tend to be indifferent to patriotism, personally uninterested in religion, and not very concerned about law-breaking by citizens.

BUT WHY do such people tend to be such dogmatic "libertarians"? The ideological associations are so familiar, it is easy to forget how essentially incongruous they really are. Why do people who would trust government officials to control the allocation of vast resources with sensitivity and selflessness so often insist that government can never be trusted to distinguish unorthodox critics from inflammatory hate-mongers, or risqué entertainment from sadistic pornography? Why do people who insist that there can be no harm in a high-school teacher touting radical political causes, or flaunting a "gay" lifestyle, object so strongly to any display of religious symbols in public schools? In general, why do those who boast of their determination to transform society through government action like to regard themselves as the greatest champions of liberty? If one

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looks at other Western democracies, there is no counterpart to the ACLU, certainly not among social democrats. And even in this country, this kind of "civil liberty" politics was virtually unknown before the 1930s and certainly did not gain much momentum in the courts before the 1960s.

How did this "civil liberties" complex begin, then? Originally, it was a useful screen for protecting Communists. It is no longer respectable to mention this today, but Roger Baldwin, the founder and guiding spirit of the ACLU in its early decades, was occasionally quite candid about the matter. As late as 1934, noting that "the Soviet Union has already created liberties far greater than exist elsewhere in the world," Baldwin explained his defense of mere bourgeois civil liberty in America in these terms: "If I aid the reactionaries to get free speech now and then, if I go outside the class struggle to fight against censorship, it is only because those liberties help create a more hospitable environment for working class liberties . . . . When that power of the working class is once achieved, as it has been only in the Soviet Union, I am for maintaining it by any means whatever. Dictatorship is the obvious means in a world of enemies, at home and abroad."

To be sure, Baldwin, like many others, cooled considerably toward Soviet Russia after the Hitler-Stalin pact, and in the 1940s he actually supported the purge of unrepentant Stalinists from the ACLU national executive. But a lingering regard for the revolutionary left—in later decades no doubt more sentimental than conspiratorial—has continued to fuel "civil libertarian" fervor in some quarters, as can be seen in careers like that of Leonard Boudin, general counsel of the National Emergency Civil Liberties Union and registered agent for the government of Castro's Cuba.

For most post-New Deal liberals, however, the appeal of a "libertarian" approach to civil liberties doubtless lay elsewhere. For some, insisting on absolute freedom for expression or conscience was a psychic (or at least rhetorical) compensation for their support of an unprecedented expansion of administrative power in Washington. It was doubtless an impulse of this kind that led FDR, near the end of the New Deal, to sponsor construction of a Jefferson memorial in Washington and to seek to identify the party of big government with the Jeffersonian ideal of the free-thinking, independent farmer.

BY THE 1960S others—and perhaps many of this group, as well—came to rely on "libertarian" postures as a way of making self-government safe for cosmopolitan sensibilities. The prime thrust of the new "civil libertarian" litigation, after all, was seldom to constrain the growing power of the central government, but instead was directed to preventing provincial majorities in states and localities from enacting *their* moral standards into law, when these conflicted with those of the national elite. People who regarded

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pornography as a harmless indulgence—but any mention of God in the schools as a dangerous influence—persuaded themselves that their preferences were those of the Constitution. Under the banner of "civil liberty," unenlightened provincials who saw things differently could be forced to submit—without the awkwardness of a direct political battle. From this point of view, there was no inconsistency at all in promoting big government along with an extreme, "absolutist" approach to civil liberties: Both were instruments of the same effort to remake American society in the image, or at least according to the vision, of a governing elite, whether this involved a civil rights bureaucracy to impose its notion of proper racial balance, or a judicial censor to certify the secular purity of a local public school.

Doubtless there remain some who believe that activist social regulation and an activist approach to "civil liberties" all serve the same unassailable aim of enhancing individual opportunity. But beyond a certain point, of course, one man's opportunity becomes another's oppression. And when even the ACLU presents "civil liberties" as a catalog of group rights, it no longer makes much sense to treat civil liberty issues any differently from the values and competing interests of everyday politics. Indeed, as the ACLU has added new groups to its banner, it must encounter painful conflicts within its own camp (for example, between radical feminists and defenders of pornography). Perhaps the convergence of several such conflicts on the issue of free speech accounts for the curious omission of the topic from the current volume. Whatever course the ACLU itself pursues, though, we are likely to see an erosion of support for its traditional absolutist positions on "tolerance" issues, among "opinion elites" and within the courts.

McCloskey and Brill inadvertently provide several hints about this. Their surveys reveal that the mass public is much less concerned about domestic political "subversion" than it was in the 1940s and 1950s. The last "red scare" is now several decades behind us—as is the last period in which any significant number of intellectuals or would-be "opinion leaders" flirted with conspiratorial or anti-democratic organizations. In the present climate, efforts to enforce minimal norms of decency in public expression may no longer trigger immediate defensive concerns about "witch hunts," even among liberals or activists on the left. At the same time, there seems less compulsion now to identify the welfare state with a pious regard for individual liberties. After several decades of experience with the welfare state, even its sharpest critics tend to depict it as a burden on prosperity or creativity rather than as a sinister threat to liberty.

Finally, in what is perhaps the most interesting finding, McCloskey and Brill report little difference between different regions of the country, or even between urban and rural samples on their measures of "tolerance" or "support for civil liberties." Comparisons with poll data from the 1940s and 1950s do confirm the impression

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that the country is becoming more homogenous and in general more cosmopolitan and tolerant (if not quite enough so to satisfy the standards of McCloskey and Brill). With any luck, debates and decisions on civil liberty issues will, in the coming decade, offer closer consideration to the requisites of civility and less posturing about the demands of liberty. A decade from now, the polling follow-up to *Dimensions of Tolerance* may discover that opinion leaders and elites have almost caught up with the good sense of the mass public.

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Introducing the Pre-Keynesians

RICHARD N. LANGLOIS

***Mark Casson:* Economics of Unemployment: An Historical Perspective.** *MIT Press. 298 pp. $35.00.*

YOU KNOW about the Keynesians. You've heard about the Post-Keynesians. Now meet the Pre-Keynesians.

Actually, you may already know these writers by another name. They are none other than the doctrinaire and dim-witted "classical school" immortalized in sarcasm by John Maynard Keynes in the *General Theory*. You remember: These are the guys who believed "supply creates its own demand" and could not recognize economic truths that the common laborer finds intuitively obvious. These are the guys who blindly and heartlessly opposed deficit spending in the depths of the Great Depression. You remember.

In his latest book, the prolific British economist Mark Casson has rechristened this school the Pre-Keynesians. One can only be sympathetic with his objectives. For the inter-war economists who have been forced to bear the name "classicals" are not on the whole guilty of the stupidities—or even representative of the economic beliefs—with which Keynes charged them. And perhaps a new baptism will help clear their names. That Keynes was often a sloppy and self-serving intellectual historian is not news, of course. But Casson is up to more than rewriting intellectual history; his is a comprehensive attempt at vindication. Beyond setting the doctrinal record straight, he wants to establish the Pre-Keynesians as precursors of certain contemporary trends in unemployment theory and to assert the relevance of their ideas to economic policy (both past and present). In the first of these tasks he is largely successful, even if this success is not quite the triumph he seems to think it is. In the second task he has also succeeded, if in a somewhat more qualified way.

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Who were the Pre-Keynesians? The leading figure—for both Casson and Keynes—is A. C. Pigou, Keynes's senior colleague at Cambridge, who occupied the chair once held by Alfred Marshall. For Casson's purposes, the group also includes Edwin Cannan and Henry Clay. And what did they believe? The Pre-Keynesian theory of unemployment had two interrelated aspects. The first was an insistence that, in the medium to long run, unemployment is what we would now call a "microeconomic" phenomenon rather than a "macroeconomic" one. The second aspect was a concern with the *structural* nature of unemployment.

THE IDEA of macroeconomics as distinct from microeconomics is something that the twentieth century learned from Keynes. Before the *General Theory*, no one thought to distinguish "micro," the theory of prices and markets constructed from considering individual behavior, from "macro," the behavior of the economic system "as a whole." This is not to say that economists before Keynes were unconcerned with such macro problems as fluctuations in income and employment; there was in fact a lively practice in business cycle theory, associated with Hawtrey, Hayek, and Robertson. These writers were interested in how a basically healthy microeconomic system could "get sick" and display disturbing macroeconomic symptoms. The focus of these diagnostic investigations was typically money—the blood of commerce, as the mercantilist writers used to say. Money is a commodity like any other, and thus susceptible to microeconomic analysis; but it also has some unique properties, notably its liquidity, that make it a potential source of trouble. To put it crudely, money helps tie the system together, but it does so only imperfectly under some circumstances. (In Hayek's theory, for example, injections of newly created money can send misleading signals to the investment community, distorting the structure of investment in a way that leads to an eventual recession.)

To say that Casson's Pre-Keynesians see unemployment as principally a microeconomic phenomenon is to say that they do not see money as causing difficulties in the medium to long term. (This is the kernel of truth in Keynes's depiction of the classicals.) As a consequence, persistent unemployment ought to be impossible unless there is something (other than money) playing havoc with the pricing system. Unemployment means that the price system is not bringing the supply of labor into balance with the demand: There must be a monkey-wrench in the machinery. Pigou and his followers located the trouble in a "market failure," the ability of labor unions to keep real wages above the market-clearing level. This means that monetary policy will not help cure unemployment, since unions will soon see through inflation and take it into account in making their demands. Similarly, fiscal policy will be ineffective, since government spending will just crowd out private spending, leaving employment unchanged.

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To say that unemployment is largely a macroeconomic phenomenon is, by contrast, to say that money is not doing a good job holding the system together. Because of the presence of money, the system may be sending out misleading signals, and markets—like the labor market—may not clear *even without* any microeconomic "market failures." This is very much the spirit of Keynes's diagnosis. The precise theoretical structure of the diagnosis is, however, far less clear. The *General Theory* is an Alice-in-Wonderland world for the theorist as much as for the intellectual historian. The late Joan Robinson and the Post-Keynesians take Keynes's message to be that money ties the system together not at all, and thus that the economy simply does not work. UCLA economist Axel Leijonhufvud has argued that the "real" Keynes is a somewhat more moderate figure, one in the spirit of the earlier business-cycle theorists. The standard interpretation has long been that Keynes's theory hinges on two pivots: sticky (money) wages and the liquidity trap. It is this last interpretation that is of interest, since that is the view of Keynes adopted by his followers and incorporated into the so-called neoclassical synthesis after World War II.

THE LIQUIDITY TRAP, an idea developed by Keynes's followers rather than by Keynes himself, is a kind of formalization of the old Mercantilist fear of hoarding. It was Pigou who showed why such a "trap" could never cause the system any problems. Because the price level would be falling at the same time, the erstwhile hoarders are getting wealthier in real terms, which, on Keynes's own assumptions, leads them to stop hoarding and start consuming; and that creates the aggregate demand necessary to restore full employment. With the demise of the "trap," the stickiness of money wages became the sole theoretical underpinning of Keynesian (macroeconomic) unemployment.

And that brings us back to the Pre-Keynesians. For it suggests why Casson finds it so easy to reinterpret Pigou and company in modern terms: They were essentially modern neoclassical Keynesians on this issue. As Casson well documents, the Pre-Keynesians—contra Keynes—always agreed that rigid money wages (caused by "money illusion," the assumed tendency of workers not to take changes in the cost of living into account when making labor-market decisions) could cause unemployment in the short run. The only possible source of disagreement would be the length of the "run" over which money wages are sticky.

Much of Casson's effort is devoted to showing how the Pre-Keynesians anticipated such modern ideas as labor-market search theory. And much of this argumentation takes the form of a rational reconstruction of Pre-Keynesian doctrines in terms of modern economic modeling, with an admission that there is often as much Casson in the models as there is Pre-Keynesian. But, here again, it should not be wholly surprising that the Pigovians are so easily recast. Search

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models and related variants are really extensions of Marshallian price theory, and it is hardly startling that Marshall's sucessor should fit so well into that mold.

Most economists believe that the proof of the theoretical pudding is solely in the empirical eating. (They are almost alone among scientists in still believing this.) And Casson does not disappoint on this score. He presents empirical results showing that the movement of real wages in Britain during the depression is consistent with Pre-Keynesian theory. If correct, this means that the real wage must have played some role in the inter-war unemployment problem, even though it does not prove that unemployment had no "macroeconomic" causes in addition. Casson is on stronger ground in suggesting that *recent* unemployment problems are better explained by Pre-Keynesian than by Keynesian (demand deficiency) hypotheses. (This empirical work is potentially the most controversial part of the book, and for some economists potentially the most interesting.)

So, Casson has done his work well in making moderns of the Pre-Keynesians. Indeed, he may have done his work too well. For, to the extent that one thinks that modern theorists have overlooked some interesting aspects of macroeconomics (in the sense I have been using that word), then awarding them the mantle of modernity may be a thin and watery sort of vindication. As may be obvious, my own taste is to find Leijonhufvud's Keynes and the business-cycle theorists like Hayek and Robertson deeper and more intriguing than either the Pigovians or the modern neoclassicals. But status as a neoclassical is still no doubt an improvement over playing Goofy, Dumbo, and Pluto in what one historian of economic thought calls "the Walt Disney version of inter-war economics."

THERE IS MORE to the Pre-Keynesian view of unemployment than merely the assertion that real wages are too high. Indeed, there is more to their position than merely upholding microeconomic "market failure" over macroeconomic system-failure as the cause of persistent unemployment. The Pigovians were concerned centrally with the *structural* nature of unemployment, and this is where they —and Casson—are at their most interesting.

Keynesians and monetarists are united in a homogenized view of the economy: They worry about the level rather than the composition of demand, about the supply rather than the distributional pattern of money. This is often a useful theoretical simplification. But it disguises the fine structure of the economy, and obscures the lessons to be learned from studying that structure. The Pre-Keynesians, by contrast, saw unemployment as arising largely from a kind of sectoral imbalance. The economy is composed of new and growing industries on the one hand and old and declining ones on the other; unemployment arises not because there are too few employment opportunities but because, for various reasons, there are impediments to workers moving from the declining industries to the grow-

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ing ones. Some of this unemployment is merely "frictional," in that it arises because the process of worker mobility is not costless and instantaneous; some of it is "natural" unemployment, in that some workers would rather suffer at home than uproot themselves to move elsewhere; and some of it, to the Pre-Keynesians, is truly "involuntary," in that it arises because the real wage in the declining sector is too high. Here Casson invokes search theory to good effect. Even though the prospects of getting a union job in a declining industry are not very good, the high pay induces workers to spend time searching rather than moving to the growing sector. Unemployment benefits can have a similar effect, since they lower the cost of waiting for a rare but high-paying position.

Casson may well be right in seeing his Pre-Keynesians as incipient search theorists. But for me his description of their views struck a much louder and quite different modern chord. Reading Casson on the structural problems of inter-war Britain is like nothing so much as reading Robert Reich on the problems of the present-day American economy. We get the same story about a maturing economy, about the decline of the staple industries, about foreign competition catching up with the once-undisputed economic champion. We even hear the same tale about the demise of crafts-dominated production in favor of managerialism.

Looked at in the right light, this comparison is not, perhaps, too unreasonable. Reich argues that economic good sense and a "social conscience" ought not to be incompatible, and that there is a false choice between laissez-faire and government planning (even if in the end his compromise position is simply government planning). The Pre-Keynesians (especially Pigou) were also economists with a "social conscience." Pigou upheld a raw and old-fashioned brand of utilitarianism he learned from Henry Sidgwick at Cambridge. And his concern with "market failures"—a notion for which he is largely responsible and from which the profession is only now slowly extricating itself—signals a conception of the government as microeconomic tinkerer, whose job it is to correct the deficiencies of the market's "natural tendencies."

According to Casson, Pre-Keynesian industrial policy took four forms. One was industrial transference, which meant encouraging workers to migrate by reducing the transaction costs of moving to the growing sector. Retraining programs might be an example of this. (Britain tried a policy of this sort in the 1920s, and it was evidently a dismal failure.) Other policies included employment subsidies and selective protection, both of which would work only in the short run and would require an astonishingly precise tinkering ability. A fourth policy was rationalization, which was also a form of selective protection. It involved the consolidation of production into monopolies to achieve economies of scale, coupled with price discrimination between a protected home market and a competitive world market. All of these policies, or their close relatives, have

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raised their heads in the recent American industrial-policy debates. Interestingly, the rationalization idea is the opposite of what Reich recommends: He argues for abandoning mass production to Japan and the Third World in favor of high-value-added specialty production. The most Reichian policy suggested for inter-war Britain is one the Pre-Keynesians neglected (mistakenly, Casson thinks): selective investment by the government.

IN EXPLAINING the eclipse of the Pre-Keynesians in the intellectual marketplace, Casson stresses the peculiar exigencies of the times and on the personal characteristics of his protagonists. If, in the end, Reich is more "social conscience" than economic good sense, the Pre-Keynesians were the other way around. They were hard-headed economists, Casson implies, too proud to change their views for reasons of expediency—an attitude with which Keynes was never burdened. The times called for quick action (or so it seemed), and the Pre-Keynesians could only offer policies good in the medium run. Indeed, the Pre-Keynesians were often ambivalent toward their own schemes: They distrusted politicians, and recognized that the best intentions could easily be distorted beyond recognition in the jet-wash of interest-group politics. Moreover, they lacked the debating skills and political savvy that Keynes wielded so effectively. There is certainly much to this view of the Pre-Keynesians. But the nature of their approach itself must also share in the blame for their failure.

The Pre-Keynesians were indeed economists of the medium run. To put it more strongly, they were economists of the *ad hoc* and the in-between. For example, their real-wage-rigidity theory of unemployment relies on what are sometimes mistakenly called "institutional" factors—like government benefits policy and the strength of labor unions—that are external to their economic models. Unlike Keynes, whose explanation comes from within the model itself, the Pre-Keynesians grafted on explanations from the outside. The same, in the end, is true of their structural analysis. Pre-Keynesian analysis never explains *from within* why there are declining industries, why there are growing ones, or how institutions and policies influence the structural development of industry. Casson's conjecture, that such developments all have to do with the life-cycle of firms, seems to me on track; but this is nowhere incorporated into his theory. There is a powerful aesthetic component to theory choice, and that may ultimately have contributed nearly as much as personal or political factors did to the Pre-Keynesian eclipse.

How, ultimately, are we to view the Pre-Keynesians? If we are looking for a branch of the economic family tree on which to graft an exciting new theoretical shoot, then we are probably better off looking elsewhere. But this is not to say the Pre-Keynesian theory is wrong or useless. Its in-between character is part and parcel of the Marshallian tradition, and reflects both its weaknesses and its characteristic strengths. There *are* in fact various monkey-wrenches in

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the economic works, labor unions and a multitude of government policies no doubt among them. The Marshallian tradition is certainly helpful in understanding their effects and implications. And Casson's book is a splendid introduction to, defense of, and elaboration on that tradition.

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Leadership and the "Confidence Gap"

JAMES PIERESON

Seymour Martin Lipset and William Schneider: **The Confidence Gap: Business, Labor, and Government in the Public Mind.** *The Free Press. 434 pp. $19.95.*

James MacGregor Burns: **The Power to Lead: The Crisis of the American Presidency.** *Simon and Schuster. 288 pp. $16.95.*

Don K. Price: **America's Unwritten Constitution: Science, Religion, and Political Responsibility.** *Louisiana State University Press. 202 pp. $19.95.*

IT HAS NOW been more than five years since Jimmy Carter warned the American people of "a crisis of confidence" that, he said, "strikes at the very heart and soul and spirit of the national will." He pointed to a growing gap between the people and their government, and to a growing disrespect for government, schools, churches, and the news media. This new mood posed "a fundamental threat" to American democracy, and impaired his own capacity to lead the nation.

There was an irony in Carter's plea. Elected as an outsider running *against* the government, he then had to defend his record in the face of a public skepticism he himself had been encouraging. In pointing so openly to "the confidence gap," Carter established a major theme of the 1980 election campaign—a theme exploited by Ronald Reagan, in whose hands the "crisis of confidence" was turned into the "crisis of liberal governance." For Reagan, Americans had lost faith not in themselves, but in a particular approach to public policy.

The issues of "trust in government" and the "crisis of confidence," so decisively settled politically in the 1980 elections, have received scholarly treatments in three recent books. Seymour Martin Lipset and William Schneider examine the question in terms of public opinion, James MacGregor Burns in terms of the institutions of gov-

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ernment, and Don K. Price in terms of political customs and beliefs inherited from the past.

LIPSET, a senior fellow at the Hoover Institution, and Schneider, a resident fellow at the American Enterprise Institute, have consulted hundreds of public opinion surveys gathered by professional polling firms between 1935 and 1982 in an effort to track the changing opinions of the American people toward their leaders and institutions. Lipset and Schneider demonstrate convincingly that, beginning sometime in the mid-1960s, Americans in great numbers began to lose confidence in the leaders of key institutions. The collapse of confidence was not limited to leaders of political institutions, but extended as well to leaders of corporations, the press, organized labor, and the military. In 1966, to cite just a few of the figures presented in the book, 42 percent of Americans surveyed expressed "a great deal of confidence" in leaders in Congress and 41 percent expressed confidence in leaders of the executive branch. By 1981 the numbers had fallen to 16 percent for Congress and 24 percent for the executive. Similarly, confidence in corporate leaders fell from 55 percent in 1966 to 16 percent in 1981; in educational leaders from 61 percent to 34 percent; and in military leaders from 62 percent to 28 percent. The press and organized labor were the two institutions the leaders of which were consistently regarded by the public as least trustworthy: In 1966, 29 percent expressed confidence in the press and 22 percent in labor leaders, and by 1981 these numbers were down to 16 and 12 percent respectively. By far the largest portion of the overall decline in confidence occurred in the years between 1968 and 1975. Jimmy Carter, despite his pledge to do so, was unable to reverse the trend, and, as Lipset and Schneider show, he presided over a further decline in levels of confidence.

In this same period, however, Americans did maintain their faith in their form of government, and in leading social and economic institutions. The overwhelming proportion of respondents expressed pride in America's form of government and support for democratic procedures. The authors conclude, then, that "the trend of declining trust in government is focused on the performance of government and the behavior of public officials, and not on the system itself or the institutions and norms associated with it." This distinction also holds for other institutions, such as business. While many Americans are skeptical of the motives of business leaders, few support measures to extend government control over private enterprise; at the very least, it appears that most distrust political leaders as much or more than business leaders.

Lipset and Schneider locate the causes of "the confidence gap" in events that touched all Americans in one way or another. In the early 1970s, the war in Vietnam and then the Watergate scandals eroded public confidence in political leaders. Later, economic instability, particularly inflation, began to take its toll. Interestingly

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enough, Lipset and Schneider argue that inflation was the main cause of the "malaise" of which Jimmy Carter complained in 1979. Though both inflation and unemployment cause pessimism about the present, inflation creates uncertainty about the future, while unemployment does not. People had become accustomed by 1979 to the ups and downs of the business cycle, but not to the uncertainty and open-endedness of inflation. By the late 1970s, the authors suggest, the public had lost confidence in the ability of government to control rising prices, which created fears and anxiety about the future.

Lipset and Schneider conclude their volume on a note of cautious optimism. They answer the question of whether America is facing a legitimacy crisis with a qualified "no." Distrust for leaders, they remind us, is rooted to some degree in American history and institutions, and is readily galvanized when leaders fail to cope with the kinds of problems that began to accumulate in the late 1960s. Yet such skepticism does not fundamentally threaten the legitimacy of the political order because Americans distinguish between leaders and institutions, and do not judge institutions by the failures of those who occupy them. In addition, whatever their disappointments about the course public life has taken in recent years, Americans remain optimistic about their personal lives. Such attitudes buffer institutions against the temporary failures of leaders and suggest to Lipset and Schneider that "the confidence gap" can be reversed provided that new crises do not arise in the 1980s, and that political leaders can set the nation back on a stable course.

One naturally hopes that Lipset and Schneider are correct in this assessment. Still, there are good, though highly speculative, reasons for supposing that sound leadership and stable politics may not so readily overcome "the confidence gap." The rise of the adversary class in the academy and the press, and the recent disdain among some liberal groups of liberal institutions generally, have created a reservoir of opinion predisposed by habit or conviction to think ill of American institutions and leaders, no matter how well they might perform by objective criteria. In this sense, political cynicism is at least in part a *deliberate* posture—a stand taken against the world, rather than a response to the ebb and flow of events. It may thus be somewhat impervious to improvements in objective conditions and more deeply entrenched among certain groups than the polling data alone suggest.

JAMES MACGREGOR BURNS, longtime professor of government at Williams College and sometime Democratic party activist, takes a different approach to the problem of leadership in *The Power to Lead*. Burns, in contrast to Lipset and Schneider, is more interested in the phenomenon of leadership itself, and especially in those institutions of government that either nourish or weaken it. He has long believed that the great weakness of the American system lies in its

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tendency for deadlock and stalemate, and in its incapacity to address problems until they reach crisis proportions. In an earlier book, *The Deadlock of Democracy*, published in 1963, he traced this weakness to the fragmentation built into the constitutional system, principally in the form of the separated powers and federalism. Strong leaders, such as Franklin Roosevelt, are temporarily able to overcome this stalemate, but they too are worn down in time by factional infighting, conflicts with Congress, the courts, or the states, and the sheer deadweight of the constitutional order. In his new book, Burns takes these themes up again, and advances several proposals which he believes may strengthen presidential leadership.

His thesis is familiar and simply put. The presidency is the focus of political leadership in the United States, but our institutions are arranged such that they undermine the efforts of presidents to gain the sustained support needed to exercise such leadership. The chief barriers are, first, the dispersed powers provided for in the constitutional system itself, and second, the party system, which is too weak to consolidate the powers the Constitution has separated. The parties once supplied such glue as was necessary to bind these powers together, but today they only make the situation worse. Presidential candidates, armed with media consultants and independent financial contributors, can now seek party nominations without consulting party leaders, and voters are more and more cut loose from attachments that once bound them together in a common purpose. The result is a "plebiscitary presidency" in which presidents try to govern through media-dominated relations with the public. The trouble, he says, is that "plebiscitary leadership is classically short-run, unstable, ineffective [and] irresponsible." Thus, he concludes (no doubt thinking of Jimmy Carter), our presidents are able campaigners but weak leaders.

Burns proposes, as remedies for this condition, a series of structural reforms intended to modify the separation of powers along the lines of a parliamentary system, and to transform the political parties into disciplined institutions guided by clear ideological principles. He would strengthen ties between the President and Congress by adopting constitutional amendments to create a "team ticket" —under which voters could cast a simultaneous ballot for president, vice-president, senator, and representative—and to permit sitting members of Congress to occupy positions in the cabinet. He rejects the idea of a single six-year presidential term, for the reason that it would further undermine presidential accountability. Party organization, he argues, should be strengthened by replacing presidential primaries with party caucuses for selecting convention delegates, a move he believes would augment the power of party activists.

BURNS FRANKLY ADMIRES the framers of the Constitution, who boldly engineered a new plan of government to replace the weak and ineffective Articles of Confederation. But he does not

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think so highly of the document they created. He calls for a contemporary expression of the Founders' "transformational leadership" —their ability to see beyond existing arrangements and construct a new political order—this time directed to the end of undoing the institutional cobwebs the Founders left behind. Ronald Reagan, he acknowledges, provides one example of such leadership: He has demonstrated the power of conservative ideas, and has turned the Republican party into an instrument of these ideas. Yet Reagan, in Burns's view, is too much guided by narrow free-market ideas, and is thus an unlikely custodian for the agenda laid out in his book. Burns, frankly acknowledging his partisanship, places this job in the hands of "liberals, leftists, and radicals" working within the Democratic party to move it radically away from the centrist and incremental course the party has heretofore followed. The Democratic party, so transformed, will offer a genuine alternative to conservative Republicanism, and mobilize to its side millions of potential voters currently alienated from the political process. By sharpening the lines of conflict between the parties, reformers will strengthen the hand of the presidency, as the incumbent will head an ideologically united party supported by a majority of Americans.

The Power to Lead is a passionately argued book, displaying the broad learning about American history and politics one has come to expect of James MacGregor Burns. This book, however, given over as it is to partisan polemics, is not up to the standards set by *The Deadlock of Democracy* and *Roosevelt: The Lion and the Fox*, Burns's fine political biography of FDR. It covers much familiar ground and adds little to the debates over party government and constitutional reform that have been carried on now for several decades. In addition, conceived as it was shortly after Jimmy Carter's downfall, the book's preoccupation with the failure of presidential leadership seems dated. There has been a manifest contrast between Carter and Reagan in presidential leadership. To assert, as Burns does, that "no leader—no matter how charismatic or politically skilled—will be able to govern effectively given the existing Constitutional framework and informal networks of power," is to take a view at once defeatist and utopian. On the one hand, nothing can be accomplished until institutions are reformed; on the other, great changes will come once reform is achieved.

Moreover, the framers of the Constitution had sound reasons, clearly expressed, for limiting the power of the state and dispersing among the three branches those powers it *was* given. They did not design complicated institutions for their own sake, but to secure individual rights while promoting popular government. Burns speaks vaguely of a wish "to expand freedom, equality, and justice in every dimension of human life," but neither gives content to these words, nor demonstrates how in practice party government or an American version of parliamentary government will realize these

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ideals. His prescription for a more ideological Democratic party, for example, would not strengthen presidential leadership so much as it would make that party less competitive in national elections. Though Burns sympathizes openly with a radical agenda, he does not call for any of the standard shibboleths of the left, such as government ownership of industry, worker co-determination, free health care, and the like. He is absorbed more by structures than programs, and this perhaps explains why his case for merely procedural reform is made with so much passion and expectation.

IN *The Unwritten Constitution*, Don K. Price, Dean Emeritus of the Kennedy School of Government, is less concerned with reform than with understanding our current problems of governance in relation to the historical development of American political ideas, habits, and institutions. Price, like many others, is concerned that our institutions produce conflicting and ineffective policies, and do not permit the responsible administration of government programs. His book, ranging widely over American and English history, presents a host of provocative ideas bearing on what he calls our "confused sources of authority."

Price argues, in contrast to Burns, that our problems of incoherent policy and divided authority are rooted not in the Constitution and its divided powers, but in those informal and extraconstitutional customs and forms that make up "the unwritten constitution." This he defines as "the fixed political customs that have developed without formal constitutional amendment." Price here includes such practices and institutions as the party conventions and primaries, the congressional committee system, the structure of the executive departments, the Executive Office of the President, and the methods through which political news is covered by the press. The unwritten constitution, even more than the formal one, "is a reflection of the basic political philosophy of the people," and thus of greater influence on the processes of politics and the substance of policy. The unwritten constitution, he suggests, has evolved in such a way as to divide authority and weaken accountability to a greater degree than was required by the Constitution itself.

Price locates the spirit of the unwritten constitution in the ideas toward authority present in America long before the Revolution. These were articulated by the religious dissenters who did so much to shape the political culture of the colonies. Their distrust of earthly authority, a part of their religion, sought expression in the elimination of establishments and the substitution for them of the objective rule of law. Their ideas produced the American tendency to view political issues in moralistic and legalistic terms, and to settle questions of authority alternately by dividing and dispersing it, or by delegating it to neutral experts, such as judges, administrators, and, later, scientists. Such deeply held opinions, says Price, "work toward

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decentralization of power by emphasizing specialized practical concerns rather than general policy, legalistic controls rather than discretionary authority, and moralistic principles rather than political compromise." The dissenters' views of authority outlived the religious impulses that generated them, and were, according to Price, handed down to those modern scientists and public policy experts who now set the agenda for discussions of political organization and re-organization.

The unwritten constitution thus continues to emphasize an 18th-century bias against strong executive leadership and coordinated administration. This is a condition that, in Price's view, can be addressed effectively only through a political consensus to amend the unwritten constitution. He would have us permit greater executive control over administration and reduce congressional intervention into the administrative process. His purpose, it appears, is to encourage the President and Congress to focus on general lines of policy, and further to encourage both to delegate narrow administrative details to the professional civil service. To this end, he would reduce the number of legislative checks on executive agencies and programs, encourage Congress to rely more on informal rather than legal checks, and, interestingly, reduce the number of political appointees in the Executive Office of the President as well as the size of congressional staffs. The latter reform is designed to strengthen administrative coordination by discouraging the detailed regulation of executive departments by the staffs of the Executive Office and members of Congress.

The Unwritten Constitution reflects an unusual grasp of both the details of administrative practice and the historical development of our political institutions. Though on the whole an impressive work, the book suffers from a few minor defects. First, the varying ways and different contexts in which Price uses the term "science" are confusing. At times he seems to refer to expertise generally, at others to government by experts, and at others to a specialized body of knowledge separate from politics. In addition, in emphasizing the influence of religious dissenters, Price fails to recognize competing influences on American ideas of authority—especially the secular doctrines of Bacon, Locke, and Hume, who contributed both to the development of modern science and to the thinking of the framers of the Constitution. Indeed, Price's argument about the relationship between science and authority may be stronger with respect to secular thinkers than to religious thinkers. But these are only minor quibbles with a serious and well-argued volume.

PRICE'S LARGER OBJECTIVES are the traditional ones among experts in public administration: to strengthen political leadership and administrative control by enforcing a clearer separation between politics and administration. Modest reforms along the lines he sug-

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gests would no doubt be desirable, and certainly preferable to proposals requiring wholesale revision of the Constitution. Still, the political forces that create administrative entanglements with Congress are unlikely to be eliminated through the minor reforms Price suggests. To some degree, these problems arise from the inability of Congress to agree on the details of national policy. Failing to reach agreement, Congress approves vague and general statutes, and delegates the difficult political tasks to the executive. Interested members of Congress naturally become involved when difficult choices have to be made. In this sense, Congress delegates conflict, not authority, to the executive, but this is the price paid to enable Congress to act at all. Administrative decisions in such a context are thus not purely administrative, but highly political. To make the problem more difficult still, administrators in the United States are frequently not neutral experts, but advocates for the programs they oversee. They are thus prepared to make political alliances with interest groups and members of Congress in order to achieve their objectives. To strengthen the separation between politics and administration, then, it would be necessary to address some of these narrower political problems.

Both Burns and Price, in concentrating on institutional and administrative reforms, fail to pay much attention to an important task of democratic political leadership—building a consensus behind a national program. The Constitution, to be sure, makes it difficult to act in the absence of such a consensus, and Burns's reforms in particular are designed to reduce the importance of consensus-building and to encourage ideological division. The checks and balances in the Constitution, however, in addition to serving important political values, require presidents to reach beyond the balky machinery of government to mobilize opinion to their side. When such a consensus is in place for a period of time, the purely institutional problems described by Burns and Price have a way of being brought under control.

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The New International Regulatory Order

MARC F. PLATTNER

Mary A. Fejfar: **Regulation of Business by International Agencies.** *Center for the Study of American Business. 108 pp. $5.00.*

Fred D. Miller, Jr.: **Out of the Mouths of Babes.** *Social Philosophy and Policy Center, Bowling Green State University. 98 pp. $6.95.*

Mike Muller: **The Health of Nations.** *Faber & Faber. 225 pp. $15.95.*

DURING THE PAST several years, interest in the issue of international regulation has begun to spread beyond the confines of obscure multilateral agencies to a much wider public. The controversy generated by the Reagan administration's negative votes on the World Health Organization's infant formula code in 1981 and the UN Law of the Sea Treaty in late 1982 even reached the evening news and the front pages. Congressional concern, stimulated by proposed consumer protection guidelines under consideration by the UN Economic and Social Council (ECOSOC), resulted in May 1983 hearings on UN regulation by a Senate subcommittee. Executive branch officials with responsibilities in the areas of international economics and international organizations are increasingly finding their time occupied by regulatory questions. Multinational corporations, having learned that their operations can be significantly affected by the actions of international agencies, are following these issues with much greater care, often hiring specialized personnel to deal with them. And consumers and other activist groups have been focusing a greater share of their energies on the international level—partly in response to finding a less hospitable climate for new regulatory initiatives at home.

Yet despite the new interest in international regulation, the scholarly literature in this area remains surprisingly thin—especially in comparison with the enormous outpouring of academic work on domestic regulation. To be sure, there are many good studies of individual international agreements or agencies, in particular of such well-established traditional regulatory organizations as the General Agreement on Tariffs and Trade (GATT). But there have been no serious intellectual attempts to think through international regulation as a whole. Such a task would indeed be a formidable one, given the incredible number and variety of organizations involved, as well as the speed with which new developments are taking place. Merely to assemble the basic information necessary for an overall appraisal of international regulation would be a considerable undertaking.

THUS THERE IS REASON to be grateful for the publication of *Regulation of Business by International Agencies*, a little report written by Mary A. Fejfar for the Center for the Study of American

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Business. Fejfar makes a useful contribution by pulling together information on a wide range of international regulatory activities undertaken not only by the United Nations and its specialized agencies, but also by the European Economic Community (EEC) and the Organization for Economic Cooperation and Development (OECD). Unfortunately, her study is far from comprehensive and not always fully accurate and up-to-date—an understandable shortcoming given the vast, uncharted field with which it deals and the fact that many of the initiatives it describes are still being negotiated.

After a brief overview, Fejfar divides her report into six chapters treating various international regulations as they affect "six basic business functions: Operations, Marketing, Finance, Technology, Services, and Information." While this organizational scheme might be helpful for the practicing businessman, it offers little promise as an intellectual framework for analyzing international regulation. Better categories would focus on the purpose, source, and legal status of international regulatory efforts. Under purpose, one might identify at least three main classes: *economic* regulation aimed at establishing agreed-upon procedures or maintaining a balance of economic advantage in transnational economic activities (trade, investment, commodities, business practices); *social* regulation aimed at protecting health, safety, the environment, privacy, and the rights of consumers; and regulation of *access to resources* not under the control of any sovereign state (for example, the oceans, Antarctica, the moon, the geostationary orbit, the spectrum of radio frequencies). Of course, regulations ostensibly belonging to the latter two categories may also have protectionist or redistributive intentions or effects.

With respect to source, one would first have to distinguish regional organizations like the EEC (whose regulations often promote group integration at the expense of outside states) from broader, limited-membership organizations like the OECD or the Antarctic Treaty, and from universal organizations like the UN and its specialized agencies (whose regulations often aim at procuring special advantages for developing nations). Yet the various UN bodies also differ enormously among themselves in terms of voting structures, traditions, technical expertise, and degrees of politicization. Thus the question of whether a particular regulatory issue is taken up in the United Nations Conference on Trade and Development (UNCTAD) or GATT is not merely a jurisdictional squabble but is likely to have a decisive effect on the substance of any agreement. Finally, with regard to legal status, international regulations run the gamut from legally binding treaties to purely voluntary codes and guidelines (although the latter often eventually come to be embodied in national legislation).

IN A PREFACE to *Regulation of Business by International Agencies*, Murray Weidenbaum refers to Fejfar's study as being "relatively free of value judgments." Unless one leans very heavily on the qual-

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ifying adverb, this is a dubious characterization—and one that certainly would not be accepted by regulatory enthusiasts. Reflecting an attitude expressed in Weidenbaum's preface, Fejfar generally views international regulations as so many hindrances to business efficiency, promoted by the Third World in pursuit of a redistributionist agenda. There is no question that this aptly describes much recent UN activity in the field, but it does not suffice as an appraisal of international regulation as a whole.

In part, Fejfar is able to sustain this perspective by omitting from her study regulatory policies that are not ideologically controversial within the business community—examples would include the maritime and air safety regulations of the International Maritime Organization and International Civil Aviation Organization, and the work on food product standards of the joint WHO-Food and Agriculture Organization Codex Alimentarius. But even within her study she presents information that calls into question her persistently negative view of international regulation. Thus GATT is praised as being "rooted in principles of free market efficiencies." Recent efforts within the World International Property Organization to weaken international patent protection under the Paris Convention are rightly criticized—but this of course implies that the Paris Convention is a desirable instrument of international regulation. Fejfar notes that the United States, whose strict anti-bribery laws put its companies at a competitive disadvantage abroad, has been pushing for the adoption of a UN-sponsored International Agreement on Illicit Payments. She expresses concern over efforts to renegotiate the Antarctic Treaty into a UN agreement resembling the Law of the Sea Treaty—once again, presumably, recognizing some virtues in the existing Antarctic Treaty arrangements.

In sum, there are many good reasons for various kinds of international regulation, even from a free market or pro-business perspective. Appropriate international regulations may foster rather than hinder the efficient operation of international business by reducing national barriers to trade and investment, by standardizing conflicting national regulations, and by providing a more secure legal framework for property rights. Moreover, rapid technological advancement and progress toward a more integrated global economy will only increase the need for international regulation in the years ahead.

The real problem lies with the institutions that do the regulating—particularly the United Nations and some of its specialized agencies. All those UN bodies structured on the principle of one-nation-one-vote are dominated, to a greater or lesser degree, by the Group of 77, the economic caucus of the developing countries. The prevailing ideology of the Group of 77 (and of most UN bureaucrats) is hostile to free markets and to multinational corporations, and in favor of global redistribution. As a result, UN regulatory initiatives are too often aimed not at securing mutual benefits for all nations, but

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at promoting the ideological and economic interests of the Third World at the expense of the West.

TODAY, with many of the regulatory thrusts proclaimed in the Group of 77's 1975 program for a New International Economic Order having been delayed or stalemated, the "hottest" area of new activity is in social regulation. Multinational corporations in the pharmaceutical, chemical, and food industries are under siege in the international agencies, with a coalition of activist groups, UN staffers, and Third World representatives pressing the attack. The 1981 WHO infant formula code was the first great victory for the coalition, and its next major target is a similar code for the pharmaceutical industry. According to a newspaper report by journalist Andrew Radolf, a UN staffer called the infant formula code "a precedent for UN regulation of multinationals," and predicted that the "battle to 'break the monopolies' of the pharmaceutical companies 'will make the breastfeeding issue look like a pebble in the pond.'"

A good sense of the range of issues and passions involved in the controversy over international social regulation is conveyed by two recently published studies embodying radically different perspectives. *Out of the Mouths of Babes* by Fred D. Miller, Jr. offers a retrospective look at the infant formula debate from a libertarian point of view. And *The Health of Nations* by Mike Muller, whose earlier book *The Baby Killers* helped to heat up the infant formula battle, presents an indictment of the international pharmaceutical industry.

In *Out of the Mouths of Babes*, Fred Miller usefully divides into separate chapters his treatment of the ethical and the factual issues surrounding the infant formula controversy. With regard to the latter he concludes on the basis of a fairly convincing analysis that the case against the infant formula manufacturers is "not substantiated by the preponderance of scientific research." On the ethical side, he offers a rather general defense of the superiority of a natural rights/individualist/free market standpoint to a utilitarian/collectivist/paternalist standpoint. This abstract moral argument is not likely to persuade the as yet unpersuaded, but, like Miller's study as a whole, it is well-written, clearly argued, and reasonably dispassionate in its treatment of opposing views.

The greatest weakness of Miller's book is its lack of attention to what might be called the political issues—in particular, the proper role of international agencies. Thus he criticizes both the U.S. State department and Abbott Laboratories (a leading U.S. producer of infant formula) for not basing their opposition to the code squarely on the principle of individual rights, and is particularly outraged by Abbott's public statement that "each government should promulgate such safeguards as necessary to protect breastfeeding." Now, while one may believe that infant formula companies ought to be entitled to advertise and market their product everywhere, the denial of this opportunity by a national government could hardly be

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considered a violation of a fundamental human right. Indeed, under international law any nation would clearly seem to have the sovereign right to ban entirely the sale of infant formula.

The real political issue is what business an international agency has promulgating a code to regulate the marketing of infant formula. There is no intrinsically transnational dimension to the infant formula issue, no need for all countries to adhere to the same policies. There is nothing in the code that could not just as well be achieved, for better or for worse, by domestic legislation alone. Moreover, although public justifications for the code all rest on the special disabilities (ignorance, illiteracy, etc.) of poor mothers in developing countries, nothing in the language of the code restricts its application to the Third World. As so often happens in the UN, what begins as a frankly paternalistic program to counter the special problems of developing countries is transformed into a general declaration of principles with universal applicability. Of course this does not trouble the most ardent proponents of the code, whose real aim is advancing a political agenda of centralized economic planning and opposition to multinational corporations. And for those with such an agenda, the UN agencies with their Group of 77 majorities are a tempting target.

MIKE MULLER'S *Health of Nations* reveals the kind of thinking behind much of the movement for international social regulation. The jacket blurb describes his book as "a fascinating and frightening investigation—and exposé—of harmful practices perpetrated in the Third World by large multinational drug companies," and adds that the "cynical and irresponsible" activities of these companies "have caused widespread suffering, mutilation, disfigurement and even death." Both the tone and substance of Mr. Muller's book sometimes correspond to this description. He begins with an anecdotal treatment of the drug safety issue and devotes a chapter to the "market power" of the multinationals. Yet he is aware that charges of excessive concentration in the pharmaceutical industry ("just twenty-five companies accounted for nearly half" of worldwide manufacturers' sales) are hardly persuasive, and admits that "most of these companies are relative dwarfs beside the giant corporations which command the Western world's economy." Similarly, he acknowledges, "it may already be that the majority of ineffective and dangerous drugs are sold by the national companies of the developing countries or by the multinationals' other [i.e., Eastern European] competitors." With more surprising candor, he notes that "adverse effects occur relatively rarely and calls of foul play on grounds of safety alone are somewhat peripheral to my central concern."

As he makes clear, Muller's central concern is "in economic terms, whether the resources [that multinational pharmaceutical corporations] have captured would not generate more benefit to

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their consumers if applied in other ways." In the first place, Muller holds that relying on multinationals for drugs squanders precious foreign exchange and hampers development:

> The countries of the Third World have made it clear that they cannot continue to base their economies on imports of consumables like drugs, for they would need to be able to pay for them through their exports, and experience has shown that earnings from exports to the rich world are unstable and unreliable. So, rather than serve the needs of the rich, both as suppliers of raw materials and as captive customers for consumer goods, they are trying to turn their economic development around to serve the needs of their own peoples, creating internal growth and reducing expensive dependence on imported goods and unstable export markets. Their best medicine is surely the exploitation of local materials for local needs. The Third World may benefit less from the drugs themselves than from the economic development implicit in the bricks and mortar of the factories built to produce them.

As this passage illustrates, Muller's support for local production of drugs in the Third World is based on grounds not of health or safety but of economics. Moreover, it is a highly ideological and remarkably non-empirical brand of economics. If "experience has shown" anything over the past decade, it is that developing countries following export-oriented strategies have outperformed those relying on import substitution.

MULLER ALSO ARGUES that the drug expenditure pattern fostered by the multinationals is "irrational." Not only are medicines misprescribed and misused, but the developing countries spend far too great a proportion of their health dollars on "trivial" drugs such as cough and cold remedies, vitamins, and analgesics. Given the acute health problems and the limited financial resources of developing countries, their governments must step in to promote "rational policies" that focus on "primary health care." In particular, they must follow WHO's lead in limiting their use of pharmaceutical products to a short list of "essential drugs." It is not enough, however, to institute such policies in the public health-care sector alone (where, as Muller indicates, the multinationals seem willing to cooperate in supplying essential drugs at low prices). For to allow a wider choice of drugs in the private sector would create a "two-tier world," in which

> the extravagance of the uncontrolled market for the rich would be a permanent advertisement for the multinationals, a goal to which the poor might aspire. The poor peasant farmer will not believe that the basic drugs he gets from the health centre are as good or better than the expensive vitamin tonic which the prosperous village shopkeeper claims is the source of his well being. . . . It will work on an international scale as well. As long as rationally chosen essential drugs are tarred with the brush of poverty, countries with rising incomes will be vulnerable to the suggestion that they are getting less than the best.

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One can only conclude from this passage either that Muller does not really believe that "rationally chosen essential drugs" supply the best medical care, or that he takes a remarkably dim view of the intelligence of the poor.

Given his ideological predilections, it comes as no surprise that Muller's model turns out to be Marxist Mozambique. His book is filled with praise for its ruling party Frelimo, and its refusal to "rebuild the inequality" in medical care that had existed under Portuguese colonial rule. He approvingly quotes a Frelimo directive that states: "The nationalization of medicine and the prohibition of its practice for profit put an end to the exploitation of disease in our country." Muller's goal of a thoroughly egalitarian health care system clearly requires the elimination of any role for the private sector. Thus he regards not only the multinationals but also Third World private medical practitioners and pharmacists as obstacles to rational drug policies.

AT ITS ANNUAL MEETING in May, the World Health Assembly (WHA) passed a resolution on pharmaceuticals that, among other things, requested the Director-General of WHO "to arrange, in 1985, a meeting of experts of the concerned parties, including governments, pharmaceutical industries, patients and consumers' organizations to discuss the means and methods to ensure rational use of drugs, in particular through improved knowledge and flow of information and to discuss the role of marketing practices in this respect, especially in developing countries." This "meeting of experts" and its mandated report to the World Health Assembly in 1986 are likely to be the focal point of the most controversial international regulation issue of the mid-1980s. WHO has long played a useful and entirely proper role in fostering the exchange of information about national drug regulations among member governments; it also has a legitimate mandate to provide technical advice and assistance to developing countries. But the wording of this most recent WHA resolution indicates that it is moving—or being pushed—in the very different direction of a marketing code for pharmaceuticals. The public debate over such a code will no doubt feature horror stories of alleged misconduct by the multinationals. But as Muller's book reveals, the real aim of many of those urging a pharmaceutical code will be not drug safety or quality, but bringing to us all the blessings of "rational use of drugs," Frelimo-style. If international agencies like WHO allow themselves to be diverted in this way, they will no longer deserve or continue to enjoy the support of the United States.

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Lessons of Limits

R. SHEP MELNICK

John E. Schwarz: **America's Hidden Success: A Reassessment of Twenty Years of Public Policy.** *W. W. Norton. 208 pp. $12.95 cloth, $5.95 paper.*

Charles R. Morris: **A Time of Passion: America 1960-1980.** *Harper & Row. 270 pp. $17.50.*

TO A GREAT EXTENT, contemporary American politics revolves around competing evaluations of the politics of the 1960s and 1970s. Both Ronald Reagan and Gary Hart have denounced the "failed policies of the past," leaving Walter Mondale alone to defend the Democratic legacy of the past 20 years. The coincidence of elections and decades is, after all, far too neat for political pundits to ignore. The Eisenhower and Reagan presidencies sit as bookends to two decades of Democratic supremacy. Add to this the analogy of Vietnam to El Salvador, and the temptation to devise definitive lessons from recent history becomes irresistible. Thus the effort of political candidates to emphasize ties to key figures of the past (Mondale with Humphrey, President Reagan with Governor Reagan) or to manufacture such ties (Gary Hart with JFK) is more than a crass attempt to cash in on nostalgia. Underlying it is a desire to use personification to make sense of an era of nearly unprecedented political change.

Two new books provide thoughtful evaluations of the policies and politics of the period from 1960 to 1980. In *America's Hidden Success* political scientist John Schwarz argues that the federal government has been remarkably successful in reducing poverty, protecting the environment, and facilitating the difficult integration of the baby boom generation into the labor market. Conservative rhetoric, he argues, has not only misrepresented the facts, but has ignored the significant challenges to prosperity that liberal programs were able to meet. Former political executive Charles Morris is less partisan and more cautious. His *A Time of Passion* explores both the period's success stories—most notably civil rights—and its all too apparent failures: Vietnam, the early War on Poverty, and stagflation. He asks why American politics has produced these failures, and why it has generated so little appreciation for its own successes. He finds the answer not in partisanship, but in the prideful sense of omnicompetence that characterized the early 1960s and in the left's irrational reaction to government's failure to live up to its own promises. Morris's more detailed history serves as a helpful complement to Schwarz's polemic.

Schwarz's defense of the welfare and regulatory state has two components: an all-out attack on the claim that the Democrats

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wrecked the economy and a recounting of the benefits provided by new government programs. In his first endeavor, Schwarz provides us with some interesting statistics. Most arresting is his finding that state and federal income tax receipts increased only from 10.8 percent of personal income in 1960 to 12.9 percent of personal income in 1980. Between 1969 and 1980 the total tax bite rose from 31.4 percent of GNP to 31.7 percent. This gives considerable support to his claim that the era did not see runaway spending and taxing. However, Schwarz fails to emphasize a number of significant qualifications: the first figure does not include the huge new Social Security taxes added in the late 1970s; it ignores changes in the distribution of the tax burden as well as the costs of evasion and avoidance; and most important, it disguises the fact that income taxes increased at a rate of 20 percent while the economic pie was expanding enormously. Still, Schwarz's recitation of facts and figures makes it hard to believe that the government has singlehandedly taxed us into stagflation. One suspects that while conservatives constantly harp on the economic effects of the growth of government relative to the private sector, what really concerns them are the social and political consequences of the absolute growth of government's agenda.

Fortunately, Schwarz provides a spirited defense of the very programs that conservatives attack most frequently. Fewer people live in poverty today than in 1960 because a variety of government programs—food stamps, SSI, AFDC, Medicare, disability benefits—give resouces to those least likely to be absorbed into the growing economy. One can understand why the author emphasizes such statistics as the number of people brought above the poverty line and the decrease in infant mortality rates, while avoiding the subjects of welfare dependency and skyrocketing public and private health costs. But when he proclaims CETA a success story one has the sense that he occasionally plays fast and loose with policy evaluations.

SCHWARZ'S WANDERING from the convincing to the implausible reveals a tendency, shared by many liberals, to defend the progress of the 1960s and 1970s as a whole—despite the fact that the most important political choices occur at the margin. Schwarz's discussion of pollution control is an example. He concedes that despite huge expenditures, water quality has not improved significantly. But rather than ask what distinguishes programs that succeed from programs that fail, he resorts to anecdote (Lake Erie has fish again; whether they are edible is a question left unanswered), and then to claims that the total benefits of pollution control outweigh the total costs. The last claim is quite possibly true, but it is certainly misleading politically. Environmental benefits are relatively cheap at first and get progressively more expensive. Why should these early payoffs be used to justify later excesses and irrationalities? It is unconvincing defenses such as these that lead many voters to long for "new ideas."

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Schwarz's argument is more convincing when he arrives at America's most hidden success: dealing with the baby boom generation. Finding jobs for the 30 million additional Americans who entered the job market between 1965 and 1979 was "a towering economic challenge." Unemployment was bound to rise and productivity to decline. Moreover, government had little choice but to allow higher inflation in order to keep unemployment within reasonable bounds. Schwarz does not so much claim that American fiscal and monetary policies were successful as that we did rather well given the enormity of the challenge. He seeks "to impress upon the public the essential context within which the economy and government were called upon to operate." Schwarz implies that the worst is now behind us. But as the baby boom bulge moves along, the Social Security system moves closer and closer to crisis. As government's responsibilities grow, it seems that a good many things government cannot change create "towering challenges."

Somehow, this review of America's successes leaves one thing out: civil rights. This is a strange omission given that *de jure* segregation was eliminated "root and branch" in the 1960s, that federal legislation has helped blacks become a potent political force, and that public opinion on race has undergone a profound change. The defense of fundamental civil rights—from Hubert Humphrey's 1948 platform fight to the Civil Rights Act of 1964, the Voting Rights Act, and the desegregation of southern schools in the late 1960s—was the Democratic Party's finest hour and a tribute to American political morality. Why, then, does someone like Schwarz, who tends to oversell other projects, seem to forget this one? One suspects because admitting success might undermine current affirmative action efforts, which assume that bigots have simply become more subtle. Pity poor Walter Mondale: Not only is he unable to rest on his laurels, he is also pushed into making promises that deny the nobility of his previous actions.

CHARLES MORRIS deals skillfully with Schwarz's two major omissions, civil rights and the limits of government's control over human events. Anyone who believes that nothing has changed on the first count should read his description of the South in the early 1960s. Ironically, the most startling indication of how far we have come is his description of the coolness with which the Kennedy administration treated the race issue.

But Morris's major theme is the limit of governmental—and human—mastery over events. He attempts to show how the exaggerated sense of competence of the Kennedy and Johnson administrations—seen best in Robert McNamara and his "whiz kids"—not only helped lead us into tragic failures (Vietnam in particular), but also fed the irrationalism of the left by discrediting pragmatism and science. This is a large task, one that leads the author into analyses of John Dewey as well as the Program Planning Budgeting System,

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Kierkegaard and Dworkin as well as techniques of prison reform. While the discussions of philosophy are sometimes superficial and unnecessary, one cannot help but be impressed with the author's breadth of knowledge and his ability to relate the abstract to the concrete.

Morris is at his best as he describes the cocky faith in social engineering that pervaded the politics of the early 1960s (using the Green Berets to save democracy, winning the War on Poverty before the end of the 89th Congress), and the faddish "existentialist" revolts of the late 1960s and early 1970s. (In retrospect it seems hard to believe that anyone could have taken *The Greening of America* seriously.) His argument that the latter development was a reaction to the former has a ring of plausibility to it. For if McNamara was so smart, Vietnam meant he must have been evil and the "system" a huge conspiracy. The favorite phrase of the left was "it is not by chance that . . . ," and the whiz kids claimed to leave nothing to chance. Still, one wonders if the relationship is that direct. If someone else had run the Defense department, would students really have forsaken teach-ins for trigonometry, or Marcuse for Marsilius of Padua? The danger of writing a book that "explains" a 20-year period is that the explanation can become a bit too pat, overlooking chance events (three assassinations and a third-rate burglary) and complex institutional changes (judicial activism, the reassertion of congressional power, the decline of party loyalty). Fortunately, Morris does not strain to force his narrative into his overarching theme.

THE MORAL of *A Time of Passion* is that we must learn "the limits of our own bright ideas." This teaching is addressed to all segments of the political spectrum. A sense of omnicompetence characterized not just the New Frontier and Great Society, but critics on the left who claimed that the revolution would usher in a free and rational society. While in the 1960s it was the Democrats who ascribed economic growth to their clever fine-tuning, today the Reagan administration claims that rosy economic figures resulted from its knowing how to restructure private incentives. One can deregulate an activity without depoliticizing the issue. The politicization of nearly every issue, combined with the perverse incentives of contemporary electoral politics, breeds claims of onmicompetence that are unlikely to be moderated even when conservatives win.

Still, Morris has offered good advice, which may be heeded by sober administrators, if not by exuberant campaigners. But just what, precisely, *are* our limits? Some tell us that the primary lesson of the 1960s concerns the limits of American power in the Third World. Morris indicates that these people have learned the wrong lesson and ignore the monumental atrocities of the victorious "liberation" forces in Southeast Asia. Nor does he seem to have much sympathy for Jerry Brown's California double-talk about the limits

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on "spaceship Earth." He does not even equate "limits" with the American tradition of limited government. He agrees with Schwarz that the modern welfare state has too many worthy achievements to justify a retreat to 1932.

Morris's perceptive analysis leaves us with a political dilemma. On the one hand, we must not turn policy making over to smug experts, whether they be economists, social workers, lawyers, or generals. Not only will they oversell and underproduce, but they will drain politics of the sense of right and wrong that holds a community together. On the other hand, moralistic populism is dangerous because it is so blindly self-righteous. Moreover, the issues that now confront the welfare state—whether we should increase or eliminate work incentives for the poor, whether we should substitute marketable emission rights for technology-based pollution control requirements—hardly seem amenable to simple moral judgments.

As government puts its fingers in more pies, we desperately need public servants who can master the details of complex programs, pay attention to competing demands for resources, and understand public sentiments about right and wrong. It is here that the policies of the 1960s and 1970s can best be evaluated, the lessons of recent history be assessed and applied. The U.S. has never done a very good job at training or recruiting such high level administrators, and we need them most just when left and right have conspired to cast the "bureaucrat" and "public service" in ill repute. After reading *A Time of Passion*, one is left with the feeling that a man like Charles Morris—an experienced public administrator with a sense of history and a familiarity with several specialized fields of study—could weed out some of government's failures while continuing to improve on its more successful endeavors. But on the dust jacket of his book one finds a sad sign of the 1980s: The author now works for an investment and management firm.

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Can Biotechnology Survive Us?

RONALD BAILEY

Jeremy Rifkin: **Algeny.** *Viking/Penguin Press. 312 pp. $14.75 cloth. $6.95 paper.*

Edward Yoxen: **The Gene Business: Who Should Control Biotechnology?** *Harper & Row. 230 pp. $15.95.*

Burke K. Zimmerman: **Biofuture: Confronting the Genetic Era.** *Plenum Press. 305 pp. $16.95.*

RECOMBINANT DNA first forcefully caught the attention of the public and the press in July 1974 with the publication in *Science* of a letter from a committee of eminent molecular biologists appointed by the National Academy of Sciences (NAS). These scientists urged a moratorium on certain types of gene-splicing experiments, the moratorium to last until the biological hazards of recombinant DNA research could be assessed. The letter also recommended that the director of the National Institutes of Health (NIH) develop a set of safety procedures for working with recombinant DNA molecules. A world-wide voluntary moratorium by molecular biologists then began and lasted more than two years.

This proposal set off a firestorm of protests from a wide variety of activists and critics who predicted that micro-organisms modified by this new technology could escape from laboratories, causing "superplagues" or an epidemic of infectious cancer. Some activists even urged that all such research be completely forbidden, and Congress held hearings to consider enacting some very stringent regulations on the use of recombinant DNA technology. Thus, a reasonable and responsible act of scientific self-regulation was transformed into a political issue.

In spite of the hysteria and the obstacles created by the anti-biotechnology activists, the NIH did establish the Recombinant DNA Advisory Committee (RAC). In 1976 the RAC issued a set of guidelines that specified four levels of precautionary physical containment for gene-splicing experiments, based on very preliminary assessments of the biological hazards they might pose. These NIH/RAC guidelines are applicable to all recombinant DNA research funded by the federal government, and all biotechnology companies in the U.S. have observed them voluntarily. In 1977, it was demonstrated that recombinant DNA—the sharing of genetic material between species—is a common occurence in nature. Based on this and other evidence, new risk assessments concluded that the potential harm to people and the environment was minimal. Since 1976, the NIH/RAC guidelines have gradually been relaxed, and the public furor over the danger has largely been replaced by eager anticipation of the enormous benefits that biotechnology promises.

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We are now approaching the time when the fruits of biotechnological research will be available commercially. And, once again, anti-technology activists and critics are becoming strident in their denunciations of this new industry. Although their apocalyptic visions of pandemics and environmental devastation have gone unfulfilled, some activists still hope to prohibit genetic engineering. Still others wish to hijack biotechnology's achievements and products to support their own political and social causes.

ONE OF THE MOST active and prominent members of the anti-technology lobby is Jeremy Rifkin, president of the Foundation on Economic Trends. Rifkin has been a surprisingly effective and energetic opponent of recombinant DNA research. His most recent success came in May of this year when U.S. District Court Senior Judge John J. Sirica issued an injunction forbidding the NIH to approve any deliberate-release field tests of organisms modified by recombinant DNA technology. Judge Sirica's injunction also halted an experiment by Dr. Steven Lindow of the University of California at Berkeley, in which he planned to spray a small field of potato plants with genetically altered bacteria in an effort to increase the plants' resistance to frost. This experiment would have been the first time organisms altered by recombinant DNA techniques would have been released into the environment. The director of the NIH had approved this experiment after the RAC concluded it was safe and environmentally benign. The bacteria in question live naturally on the leaves of many plants, where they produce a chemical that serves as the nucleus of ice crystals in frost formation. Dr. Lindow simply deleted the gene that produces this chemical from his bacteria. If these bacteria can replace those growing naturally on plants, it is conceivable that several hundred million dollars' worth of agricultural produce can be saved from frost damage each year. In the case of this particular experiment, it is important to note that no new genetic material was being introduced to the environment (a gene had merely been deleted), and that ice-resistant bacteria already have been created by other techniques and released without harm to the environment.

In his suit, Rifkin claimed that the RAC's failure to write an environmental impact statement on the Berkeley experiment violated the National Environmental Policy Act (NEPA). The NIH/RAC had theretofore been considering proposals for the release of genetically tailored organisms on a case-by-case basis. NEPA requires an onerous and expensive review process, which takes 18 months or more for each new proposal. NEPA has been beneficial in some cases, but very often the unreasonable delays occasioned by NEPA hearings and reports have provided few, if any, benefits. Rifkin has invoked the NEPA requirements and resorted to the courts not only because of immediate fears of the effects of this particular experiment, but also to slow, if not stop, biotechnical innovation and commercialization.

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RIFKIN SETS OUT his views on biotechnology in his recent book *Algeny*. The book is a remarkably confused document, a mixture of Marxism influenced by structuralism and a type of panpsychism espoused by Alfred North Whitehead and Teilhard de Chardin. Its overall tone is quite mystical. Rifkin is evidently upset that science has revealed so many of nature's secrets, and that mankind is making use of this new knowledge. In his view, molecular biologists have "desacralized" nature. He believes that "the goal of evolution is the enlargement of mind until it fills the universe and becomes one with it." He describes humanity's role as follows:

> Humanity is concerned with order vs. disorder and seeks to bring everything under its control. Nature is concerned with unity vs. separation and asks us to surrender to the oneness of which we are a part. Humanity seeks the elation that goes with the drive for mastery over the world. Nature offers us the sublime resignation that goes with an undifferentiated participation in the world around us.

He further argues that our technologies have set us outside the community of nature and that,

> To end our long, self-imposed exile; to rejoin the community of life. This is the task before us. It will require that we renounce our drive for sovereignty over everything that lives; that we restore the rest of creation to a place of dignity and respect. The resacralization of nature stands before us as the great mission of the coming age.

In essence, Rifkin deifies nature, and firmly believes that we sin when we tamper with it. By inducing an organism to produce something of value to mankind, we have, in his view, somehow made life irredeemably artificial. We should not arrogate to ourselves the power of improving human life through biotechnology. He asks rhetorically, "Is guaranteeing our health worth trading away our humanity?" Presumably, human genetic engineering will somehow or other make us also "artificial." But can Rifkin seriously maintain that those people who, through the aid of genetic engineering, are spared the agonies of Tay-Sachs disease or sickle-cell anemia are somehow not fully human? Though he does not say so explicitly, one gets the feeling that Rifkin's environmentalist cosmology leaves little room for human beings.

Rifkin is no Jeremiah in the wilderness; he is, rather, a very influential man. He was selected by the Congressional Clearinghouse on the Future to give a briefing to the leadership of the House of Representatives, and he advises the influential Democratic Congressman Albert Gore, Jr. Congressman Gore is the chairman of the House Science and Technology subcommittee, and has already made moves toward considering legislation to control the nascent biotechnology industry.

THERE ARE OTHER activists and critics of the biotechnology industry who do not oppose gene-splicing per se, but who think that the commercialization of its products by corporations is unaccept-

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able. Since biotechnology is a new industry without a strong lobby or political presence, these people see an excellent opportunity to impose their social and political goals on it.

Edward Yoxen, a teacher in the Department of Science and Technology Policy of the University of Manchester and an active member of the British Society for Social Responsibility in Science, is one such critic.

In his recent book, *The Gene Business: Who Should Control Biotechnology?* he writes:

> I think that the way goods and services are produced could and must be changed, so as to decrease, and, in the long, long term, abolish the inequality, poverty, exploitation, brutalisation and emotional impoverishment to be found in the present system.
>
> I would like to see biotechnology used to begin that process . . . . I wrote this book out of a sense of outrage about the way things are going, and I hope it shows.

He describes the entrepreneurial companies now entering the burgeoning field of biotechnology as participating in "free market buccaneering" that draws hapless researchers into contact with "the polluting world of venture capital, patent litigation, advertising, marketing and portfolio analysis . . . ."

Yoxen is excited by the prospects of biotechnology: new, more effective medical treatments, more abundant and nutritious food crops and animals, and new sources of renewable energy. But he is distressed that these innovations will be produced by what he regards as malevolent pharmaceutical, chemical, oil, and agribusiness corporations that are all out for a "fast buck." He claims that our current industrial system will concentrate its efforts on products for which there is a large market, and will ignore the needs of Third World nations. Yet even he recognizes the intensive research on a number of areas that will favorably affect the impoverished peoples of the developing nations: increasing the productivity of cassava, a staple in many Third World countries; vaccines for Hepatitis B and cholera, which afflict huge numbers of people living in the Third World; and treatments for the genetic disease sickle-cell anemia which is endemic to tropical Africa (and to some blacks in the United States). He misses the point that large markets, more often than not, mean that there are large needs to be met.

An example of Yoxen's line of criticism is his analysis of diabetes. While he recognizes that there is a strong genetic component to the disease, he blames the "indulgent" dietary habits of the industrialized countries for the very high rates of diabetes among their citizens. He admits that the drug companies did not create the situation, "but it should be stressed that they are complicit in its continuation." Instead of hailing the human insulin produced through recombinant DNA technology as a boon to mankind, Mr. Yoxen prefers to argue that its production has only increased people's "dependence" on commercial enterprises. Apparently, one becomes

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"dependent" if one purchases and consumes a drug that cures any disease that may afflict one; one is "independent," presumably, if one manufactures one's own curatives. Extending the logic implicit in Yoxen's analysis, one is even more "independent" if one grows one's own food, weaves one's own cloth, builds one's own house—in short, if one experiences the grinding poverty of so much of the Third World.

YOXEN ALSO WORRIES about the effects that the commercialization of biotechnology may have on the independence of universities. He argues that a university may become "a think tank for major corporations, which have exclusive access to it, rather than remaining a general social resource." But the raw information produced by university scientific research is rarely useful to most of us, at least not directly. To use the research results, resources must be mobilized to make the products and services that will benefit the general public. In democratic-capitalist societies, the gathering of resources is most efficiently and effectively done by business enterprises. In a recent Twentieth Century Fund report on university-corporate links, a task force of university administrators, research scientists, and corporate executives concluded that such links are beneficial to both parties. In particular, it was noted that funds from industry would broaden the financial bases of universities, making them *more* independent, especially from the political and budgetary pressures that so often affect federal research funding.

Curiously, while Yoxen despises the current system of production, he notes that his native country, Britain, is not keeping pace with biotechnological developments elsewhere in the industrialized world. He chalks up this failure to "the fact that historically British investment in technology has often been misguided and too late." Of course, this is not "historically" so, if one takes a long enough view. Nineteenth-century Britain was, after all, the center of the Industrial Revolution. Yoxen never attributes Britain's biotechnological failures to the kinds of policies he is advocating. The stifling regulatory environment, taxes, other disincentives to investing capital in new enterprises—all undermine the efforts of entrepreneurs to establish a new risk-taking biotechnology company in Britain. Yoxen would put the biotechnology industry into the contentious realm of politics and government where the profit motive would never intrude, and where it would probably die a-borning.

A THIRD RECENT BOOK that has addressed the issues surrounding biotechnology is *Biofuture: Confronting the Genetic Era* by Burke K. Zimmerman. Zimmerman has worked as a research scientist, a spokesman for the Environmental Defense Fund, an advisor to the House Subcommittee on Health and Environment, and as a special assistant to the director of the NIH. *Biofuture* is a thorough introduction to the field of biotechnology and the history of the

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political controversies over the use of recombinant DNA techniques. Zimmerman carefully and thoughtfully considers the public policy issues involved with the commercialization of biotechnology, and, for the most part, wholeheartedly welcomes the benefits that the speedy commercialization of this technology will bring.

However, like many people too long associated with the federal bureaucracy, he seriously underrates the damage that government regulation can do to an industry. Mr. Zimmerman believes that the scientific community overreacted to threats of regulation during the controversies of the mid-1970s. He does point out the tactical mistake made by politically naive scientists in selecting the NIH as the forum in which to develop safety guidelines for gene-splicing experiments. By involving a federal agency in rulemaking, the whole panoply of bureaucratic procedures automatically came into play, enmeshing the participants in the internecine political and bureaucratic battles between interest groups. As the author's own account makes clear, significant and burdensome regulatory action in Congress (led by Senators Kennedy and Metzenbaum and liberal New York Congressman Richard Ottinger) was avoided only because biological evidence for the common occurence of recombinant DNA in nature was demonstrated before they could act. The harsh NIH guidelines just missed being cast in legislative stone. Mr. Zimmerman, who was involved throughout these controversies, now writes with the benefit of hindsight: "In looking back, it would be hard to insist that a law was necessary, or, perhaps, that guidelines were necessary."

Unfortunately, Rifkin's successful efforts to get an injunction to halt a relatively minor experiment, and to have the courts apply the NEPA procedures to the biotechnology industry, have undercut the confidence that one can place in Zimmerman's claims for the benignity of federal regulatory efforts. In May of this year, the Cabinet Council on Natural Resources and Environment (consisting of representatives of 14 federal agencies) met to consider the proper framework for regulating recombinant DNA technology. The Environmental Protection Agency has already claimed that it has authority under the Toxic Substances Control Act to regulate the biotechnology industry. A spokesman for the biotechnology company Genentech stated in a recent *New York Times* article that the company had encountered needless delays and expense as the Department of Agriculture and the Food and Drug Administration wrangled for jurisdiction over a new interferon product designed to kill viruses that infect cattle. In that same article, a lawyer for Genentech claimed that large companies favored increased regulation because it would drive up costs for smaller companies, and perhaps "cause the small, more specialized firms to fall before any of their products can traverse the regulatory morass." Congressman Gore, in his capacity as chairman of the House Science and Technology subcommittee, has urged the EPA to take jurisdiction over most field tests

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of genetically modified organisms. Should EPA not act soon, Representative Gore has threatened to ask Congress to pass strict biotechnology legislation.

Zimmerman simply fails to see how a new industry can be strangled and deadened by the heavy hand of the federal bureaucracy. Opponents of the industry such as Jeremy Rifkin and Edward Yoxen are not so naive. If they can entangle the industry in the federal bureaucracy, they can hope to attain their political—and, perhaps, metaphysical—goals. If the anti-biotechnology organizations and activists succeed in their efforts, the pace of innovation will be significantly slowed and the enormous promise that biotechnology offers will be endangered.

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Business Ethics: Experience Preferred

WILLIAM McGURN

Tom Regan, ed.: **Just Business: New Introductory Essays in Business Ethics.** *Temple University Press. 363 pp. $29.95.*

Robert C. Solomon and Kristine R. Hanson: **Above the Bottom Line: An Introduction to Business Ethics.** *Harcourt Brace Jovanovich. 434 pp. $19.95.*

IN THE NATION that best lays claim to the title "commercial republic," the low esteem in which the populace holds the people and institutions that sustain commerce is more than a bit ironic. A few years ago, Ben Stein documented in his book *The View from Sunset Boulevard* how television fosters the stereotype of the businessman who would sell his mother for a buck, and even today—when the country is supposed to be turning right—the closest thing to a popular man of commerce is the double-dealing J.R. Ewing on "Dallas." If one were to judge by the images of television, the general rule of American economic life would appear to be "do unto others before they do unto you."

Hence we have the moral superiority some display towards those in business. In practice, though, who is untainted by the brush of self-interest? The doctor, the athlete, the journalist, the English professor—each aims in his own way to maximize his gains. In the case of doctors this may even take the form of limiting the market (reducing the number of medical school admissions, for example); and a number of those currently pursuing law degrees candidly see them as little more than an accepted vehicle for upward social mo-

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bility. Entertainers and athletes can command exorbitant wages. Yet it is the businessman—who may work significantly harder, derive less satisfaction from his job, and be paid far less than any of these others—whose ethics are repeatedly questioned.

The primary reason for this is that, despite the significant role of the commercial transaction in everyday American life, businessmen lack a well-articulated standard of fair play. Though *caveat emptor* is hardly promoted as an ideal, it is not clear exactly what American business leaders *do* defend. Doctors have their Hippocratic Oath, and even journalists have a recognized code of behavior (such as protecting the anonymity of sources).

TO BE SURE, all this says nothing about the respective morality of the individuals involved. I suspect that were people asked to rank ethically their friends and acquaintances, businessmen as a group would come out pretty well. Indeed, a Gallup/*Wall Street Journal* poll on business ethics that was published last fall touched on this curious contradiction. Not surprisingly, doctors and lawyers were thought by people to hold higher ethical standards than businessmen (though businessmen placed above congressmen). On the negative side, however, a lot more people thought lawyers and congressmen had lower ethical standards than businessmen. So, on the whole, businessmen placed in an uninspired middle.

The more interesting parts of the poll compared the attitudes of business executives to those of the general public. Here businessmen came across as far more strait-laced. Business executives, for example, showed far more qualms about such things as padding expense accounts, accepting expensive gifts from vendors, taking home business supplies for personal use, lying on one's resume, and so on. Not only was the general public decidedly more lax on these issues than the executives, they also believed that such violations occurred more frequently. Though one should hesitate to draw specific conclusions from any poll, the overall impression substantiates a general point: that there is no acknowledged standard of business conduct.

Apart from a few vague Chamber of Commerce injunctions (which usually only reiterate the law), the businessman lacks just this standard. He enters the moral fray with, at most, confused ideas about self-interest and consequently operates at a disadvantage. He is equally at the mercy of Marxist critiques of capitalism as a system and of more particular complaints of injustices in everyday business operations. Thus, our second irony: Since those who live in the world of business are unable to explain the moral basis of that way of life, the debate over the ethics of business practices falls to those—professors, preachers, congressmen—with no experience in that world. In the university (and even in graduate schools of business), where business ethics has now entered the curriculum, the moral debate takes place without hearing from the subject of the debate himself.

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THE TWO BOOKS of this review—*Just Business* and *Above the Bottom Line*—are fair examples of at least two directions these discussions of business ethics can take. The former book is a collection of academic essays edited by Tom Regan, while the latter is decidedly more down-to-earth, a beginner's book of business ethics. Both are laudable efforts, both include some telling points, yet both fall short of what is needed, ultimately at different points and for different reasons.

Just Business is a collection of essays by ten serious philosophers on such diverse topics as "Duties to One's Employer" and "Just Environmental Business." Some, like George Sher's piece on preferential hiring and Tibor Machan's on regulation, are lucidly written and finely argued. Overall, however, this book suffers from the same tendency of twentieth-century philosophy as a whole: too academic, a "parlour game" as Collingwood has called it. Depending on how one views the professionalization of philosophy, this is either a damning or marginal point.

To my mind it is a damning point; for business is more than books. Like all practical endeavors, it involves many things that can be grasped only by doing. This is a sore point with some writers; nonetheless, it is a true one. By and large, this is just the sort of concrete appreciation of commercial life absent from the pages of *Just Business*. In the biographical paragraphs on the contributors, *not one* lists any business experience. And if in fact some do have experience, and it is merely not listed, the very omission suggests what is and is not deemed important here. A glance at the footnotes at the end of each essay mainly reveals references to professional philosophy books and journals.

This does not make the contributors foolish or stupid. But it does increase the potential for their misunderstanding the nature of the beast. At its worst, this misunderstanding can take the form of Holmes Rolston III's essay on "Just Environmental Business," a silly compendium of barely-reasoned odes to Mother Earth. More serious, however, is the peculiar susceptibility of these thinkers to the notion that businessmen "control" the market, that all current arrangements are mostly arbitrary and therefore can be rent asunder with no unpleasant side effects. For example, in Adina Schwartz's essay "Autonomy in the Workplace," she cites a General Foods experiment at a Topeka dog-food plant, where tasks were "democratically redesigned." Miss Schwartz produces a *Business Week* article attesting to the experiment's phenomenal success. From this she writes:

> All people's jobs gave them significant opportunities for rationally framing, pursuing, and adjusting plans. A closer look at this General Foods experiment should now enable us, on the one hand, to dismiss certain doubts about the possibility of changing our society's arrangement for employment. On the other hand, it should allow us to indicate how extensively that arrangement must be changed if members of our society are not to be denied the opportunity to achieve autonomy.

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Thus, from the example of one plant (and with no explanation for management's reason for scuttling such a productive venture), we are supposed to conclude that it really would not be that difficult to eliminate "hierarchy" (i.e., bosses) from the workplace.

Most of the other essays, I hasten to add, do not reach quite this far. Yet even the best of them are devoted more toward correcting some ideological proposition than in setting forth standards. And Miss Schwartz's exercise is a fair example of what can happen when fevered abstractions are brought to bear upon a practical pursuit like business. Almost all those writing today about business (myself included) are writers and not businessmen, hence the obligatory paragraph about how businessmen do not appreciate the importance of ideas, should reach out more, and so on. I should like to see a few words the other way around: Do the authors of *Just Business* expect businessmen to take this book seriously? I really wonder who is being parochial here.

A MORE PROMISING ENTERPRISE is *Above the Bottom Line*. The comparative merits of this work begin with its focus as a primer for college students. In the first paragraph of the introduction, authors Robert C. Solomon and Kristina R. Hanson state an important premise: "The ethics of business life is just the ethics of people in business, and no different, basically, from ethics in general." The emphasis of this book is on the individual, with the reader asked from time to time to evaluate claims and make choices. And it is set within the appropriate context:

> In response to public suspicion of business, "business ethics" has become a distinct subject and, often, a required course in the business curriculum. But, in a more positive light, it is a subject that is beneficial and essential to business, an intrinsic part of business life. In fact, *business ethics is just the broad understanding and appreciation of business life*. It is not just criticism of business practices and business-people. It is not a series of sermons on right and wrong, as if business people were somehow peculiarly ignorant or neglectful of morals. It is not just abstract theory about the nature of business values. It is, ultimately, nothing more than careful and far-reaching thinking about a certain way of life in which money and profits play a prominent but by no means exclusive part. It is seeing the intimate interconnections between business activities and the rest of life, between business and society, between "free enterprise" and the values that such enterprise presupposes.

That is as lucid an explanation as one could wish.

In line with not treating business ethics differently from ethics in general, the authors begin with "Ethics and the Good Life," a chapter covering Aristotle's idea of the good life, wealth, hedonism, success, asceticism, and so forth, all providing a perspective for the more specific business issues that come up later. As with other chapters (for example, "Corporate Cultures and Characters"), this first is interspersed with little sidebars and quotations from major philo-

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sophical treatises and newspaper columns. Critics doubtless would complain that this is "too simplistic," that *Above the Bottom Line* should focus more on the *real* problems: multinationals, dumping, and so on. But until the fundamental ethical principles are agreed upon, those practical issues cannot be debated. *Above the Bottom Line* represents a refreshing refusal to sever business morality from the person: It sees business life whole.

NEVERTHELESS, I still think more (and better) can be done. Though *Above the Bottom Line* goes much farther than *Just Business*, there is still the whiff of the classroom about it. My proposal is this: Enlist a dozen prominent business executives, each to contribute an essay, as long or short as each wishes, on his toughest or most perplexing ethical dilemma. I have in mind something like Thomas J. Watson, Jr.'s short book on the guiding principles of IBM: something plain, easily understood, and real.[1] Originally delivered as lectures at the Columbia School of Business, Watson's book spells out the reasons for IBM's phenomenal success, primarily the core principles stating the company's respect for each individual employee and the concomitant expectations from these employees. As one who worked briefly for IBM, I can attest that the company takes these principles very seriously and has enshrined them in various corporate institutions, giving employees the right of appeal as well as increased opportunities to use their abilities. The result is a confident company, with people knowing where they stand, what is expected of them, and what their business is all about.

IBM's practices did not develop overnight, and neither will an honest business ethic. It is not something that can be imposed, ratified, or simply legislated. On the contrary, it is something that evolves slowly, largely through accumulated experience, as enough instances of problems begin to suggest general principles. Toward that end both *Just Business* and *Above the Bottom Line* make some progress—the latter more than the former—but the real work must come from within the business community itself. Only then will the ethic that suggests itself be grounded in a firm understanding of the nuances and complexities of the market, as well as in the similar complexities of the men and women who operate it. That book has yet to be written.

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[1] *A Business and Its Beliefs: The Ideas that Helped Build IBM*. (New York: McGraw-Hill, 1963).

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